S. Hrg. 109–586

# GUNS AND BUTTER: SETTING PRIORITIES IN FEDERAL SPENDING IN THE CONTEXT OF NATURAL DISASTER, DEFICITS, AND WAR

## HEARING

BEFORE THE

FEDERAL FINANCIAL MANAGEMENT, GOVERNMENT INFORMATION, AND INTERNATIONAL SECURITY SUBCOMMITTEE

OF THE

COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS UNITED STATES SENATE

ONE HUNDRED NINTH CONGRESS

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# GUNS AND BUTTER: SETTING PRIORITIES IN FEDERAL SPENDING IN THE CONTEXT OF NATURAL DISASTER, DEFICITS, AND WAR

**TUESDAY, OCTOBER 25, 2005**

U.S. SENATE,
SUBCOMMITTEE ON FEDERAL FINANCIAL MANAGEMENT,
GOVERNMENT INFORMATION, AND INTERNATIONAL SECURITY,
OF THE COMMITTEE ON HOMELAND SECURITY
AND GOVERNMENTAL AFFAIRS,
*Washington, DC.*

The Subcommittee met, pursuant to notice, at 2:42 p.m., in room 342, Dirksen Senate Office Building, Hon. Tom Coburn, Chairman of the Subcommittee, presiding.

Present: Senators Coburn and Carper.

## OPENING STATEMENT OF CHAIRMAN COBURN

Senator COBURN. The Subcommittee hearing will come to order. Senator Carper will be here. We have had a vote on the floor and I apologize to our witnesses as well as our guests for our tardiness.

Where we are—the need for priority setting. We are a Nation at war. We face trillions of dollars in unfunded liabilities of our entitlement programs. As a matter of fact, the unfunded liabilities now exceed the private net worth of the United States. We are recovering from the worst natural disaster in our Nation's history. Since 2001, the non-defense, non-homeland security government spending has increased 32 percent. Since 1998, it has grown 70 percent. Last year alone, we heaped another $2,000 per man, woman, and child in this country onto the Federal debt, individual share. The year before that, it was $1,700.

The problem addressed in this book, which is written by Peter Peterson, called "Running on Empty," argues that the appetite for spending is a fiscal train wreck waiting to happen. Well, it is here and it is time we started doing something about it.

When I visit with Oklahomans, they make it clear to me that they are losing patience with the cavalier way that we sometimes are spending their hard-earned money. There is a rumble brewing outside Washington. Americans get it. The American people understand unrestrained government growth is endangering the future quality of life for their children and grandchildren. Unlike their elected officials, they do get it. They know that when unexpected financial obligations arise, priorities must be set. We are at that stage now as a Federal Government.

I will never forget, as a freshman Member of Congress, I went to a budget hearing with Congressman Stenholm and we talked about priorities. Even though he was on the other side of the aisle, we both got it then and I appreciate him coming today. I will never forget my time in front of your committee.

They know that sacrifices must be made, yet Congress seems to live in an alternative universe, where it is OK during the time of war and natural disasters to defend earmarks for things like sculpture gardens in bills that are intended to reduce homelessness for humans, and that is just last week.

The General Welfare Clause of the Constitution could not be more clear about the finite powers of the Federal Government. When the Founders wrote in Article I, Section 8 that the government is to provide for the common defense and general welfare of the United States, they were not intending to create a nanny State that controls the lives of citizens from cradle to grave. In case there was any confusion, the Tenth Amendment should have cleared things up. The powers not delegated to the United States by the Constitution nor prohibited by it to the States are reserved to the States respectively or to the people.

The Founders worried that abuse of the General Welfare Clause would lead to too much government. Thomas Jefferson, one of my heroes, wrote, "Congress had not unlimited powers to provide for the general welfare but were restrained to those specifically enumerated, and it was never meant they should provide for that welfare but by the exercise of the enumerated powers." James Madison argues in the Federalist Papers that the enumerated powers are the finite list of Federal powers provided by the General Welfare Clause—the end of Federal authority, not the beginning.

Former Assistant Attorney General Charles Warren in 1932 complained that Members of Congress saw themselves as Santa Claus. He actually wrote a book, "Congress is Santa Claus," very interesting reading if anybody wants to go to sleep at night reading some interesting history. It seems that the problems we face today were the same problems that he described in 1932. He thought that the Congress was frivolously abusing the General Welfare Clause. He blamed this attitude for the rapid growth of government, including appropriations, and this is his words, "for any specially favored class, section, or interest which can secure a sufficient number of votes in Congress by appeals to philanthropy, by sectional bargainings, or by insistence on class privilege."

Federal spending at our current rate is unsustainable. Discretionary spending has increased, as I noted. What is more, one-quarter of total government spending now goes towards overhead. One-quarter of the $2.5 trillion Federal budget is staggering. A service sector industry such as the commercial printing industry spends roughly 10.7 percent on overhead. Why should publicly provided services require so much more in terms of bureaucracy to deliver than privately-funded services? I have argued repeatedly that today's Federal spending is not only irresponsible, but it is immoral.

The uncontrolled growth of government is responsible for the tanking of economies and quality of life for citizens of nations all over the globe. This poster shows the burden of the government in the U.S. and E.U. Let us look at one example, Germany, though there are many others, 49.4 percent of Germany's GDP is taken up now by government spending. What are the consequences of that? Their unemployment rate is almost 11 percent. Their per capita GDP now is $11,400 lower than that of the United States. The U.S. per capita economic output is 30 percent higher than Germany's. GAO's extended baseline model shows us hitting 50 percent of GDP in the year 2060 in our country. When today's high school students retire, they will face the same economic problems faced by Germany today. This is no gloom and doom prophecy, it is simply a matter of mathematical fact.

Controller General David Walker writes in "Saving Our Nation's Future" that last year, the government spent at a rate which averaged more than $1 billion per day. We are kidding ourselves if we think we are immune from most of Europe's fate.

In the early 19th Century, Congressman Davy Crockett of Tennessee took to the floor to argue against a bill that would have granted money to the benefit of a military widow. I hope you will indulge me as I read his statement into the record. This is just a portion of his learning from one Horatio Bunge.

"Mr. Speaker, I have as much respect for the memory of the deceased and as much sympathy for the sufferings of the living, if suffering there be, as any man in this House, but we must not permit our respect for the dead or our sympathy for a part of the living to lead us into an act of injustice to the balance of the living. I will not go into an argument to prove that Congress has no power to appropriate this money as an act of charity. Every member upon this floor knows that we have the right as individuals to give away as much of our own money as we please in charity, but as Members of Congress, we have no right so to appropriate a dollar of the public money.

"Some eloquent appeals have been made to us upon the ground it is a debt due to the deceased. Mr. Speaker, the deceased lived long after the close of the war. He was in office to the day of his death and I have never heard that the government was in arrears to him. This government can owe no debt for services rendered and at a stipulated price. If it is a debt, how much is it? Has it been audited and an amount due ascertained? If it is a debt, this is not the place to present it for payment or to have its merits examined. If it is a debt, we owe more than we can ever hope to pay, for we owe the widow of every soldier who fought in the War of 1812 precisely the same amount.

"There is a woman in my neighborhood, the widow of as gallant a man as ever shouldered a musket. He fell in battle. She is as good in every respect as this lady and is as poor. She is earning her daily bread by her daily labor. But if I were to introduce a bill to appropriate $5,000 or $10,000 for her benefit, I should be laughed at and my bill would not get five votes in this House. There are thousands of widows in the country just such as the one I have spoken of, but we never hear any of these large debts to them.

"Sir, this is no debt. The government did not owe it to the deceased when he was alive. It could not contract it after he died. I do not wish to be rude, but I must be plain. Every man in this House knows it is not a debt. We cannot, without the grossest corruption, appropriate this money as the payment of a debt. We have not the semblance of authority to appropriate as a charity.

"Mr. Speaker, as I have said, we have the right to give as much of our own money as we please, and I am the poorest man on this floor. I cannot vote for this bill, but I will give one week's pay to the object, and if every Member of Congress will do the same, it will amount to more than the bill asks."

I am pleased to report that Congressman Crockett prevailed that day, changing the mind of the majority of his colleagues who had been planning to vote for the measure. I hope that that same integrity will prevail in this body, as well.

[The prepared statement of Senator Coburn follows:]

***Chairman's Statement***
**Guns and Butter: Setting Priorities in Federal Spending in the Context of Natural Disaster, Deficits and War**

**Senator Tom Coburn**
**October 25, 2005**

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We are a nation at war. We face trillions of dollars in unfunded liabilities of our entitlement programs. We are recovering from the worst natural disaster in our nation's history. Since 2001, the non-defense, non-homeland security government spending has increased a whopping 32%.[i] Since 1998, it has grown 70%! Last year alone we heaped another $2,000 in debt-load on the backs of every man, woman, and child in America. The year before that, it was $1,700.

Peter Peterson argues in his book *Running on Empty* that both parties' appetite for spending is a fiscal trainwreck waiting to happen. He's right.

When I visit with Oklahomans, they make it clear that they're losing patience with the cavalier way politicians are spending their hard-earned money. There is a rumble brewing outside of Washington. The American people understand unrestrained government growth is endangering the future quality of life for their children and grandchildren. Unlike their elected officials, Americans "get it". They know that when unexpected financial obligations arise, priorities must be set. Sacrifices must be made. Yet Congress seems to live in some alternate universe where it's ok - during a time of war and natural disasters - to defend earmarks for sculpture gardens in a bill intended to reduce homelessness. And that's just last week.

The Constitution could not be more clear about the finite powers of the Federal government. When the Founders wrote in Article I, Section 8 that the government is to "provide for the common defense and general Welfare of the United States," they were not intending to create a nanny state that controls the lives of citizens from cradle to grave.

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*Chairman's Statement*
**Guns and Butter: Setting Priorities in Federal Spending in the Context of Natural Disaster, Deficits and War**

Congress, by appeals to philanthropy, by sectional bargainings, or by insistence on class privileges."

Discretionary spending has increased 32% since 2001 outside of homeland security and defense spending. What's more, one-quarter of total government spending goes toward overhead.[ii] One quarter of a $2.5 trillion federal budget is staggering. A service sector industry such as the commercial printing industry spends roughly 10.7% on overhead.[iii] Why should publicly-provided services require so much more bureaucracy to deliver than privately-funded services?

I have argued repeatedly that today's Federal spending is not only irresponsible, but immoral. The uncontrolled growth of government is responsible for the *tanking* of economies and quality of life for citizens of nations all over the globe. Let's look at one example – Germany – though there are many others. 49.4% of Germany's GDP is taken up by government spending.[iv] Their unemployment rate is almost 11% and its GDP per capita is $11,400 lower than that of the U.S.[v] The U.S. per capita economic output is over 30% higher than Germany's.[vi] GAO's extended baseline model shows us hitting 50% of GDP by 2060.[vii] When today's high school students retire, they'll face the same economic problems faced by Germany today. This is no gloom-and-doom prophecy – it is simply a mathematical fact.

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> "Mr. Speaker – I have as much respect for the memory of the deceased, and as much sympathy for the sufferings of the living, if suffering there be, as any man in this House, but we must not permit our respect for the dead or our sympathy for a part of the living to lead us into an act of injustice to the balance of the living. I will not go into an argument to prove that Congress has no power to appropriate this money as an act of charity. Every member upon this floor knows it. We have the right, as individuals, to give away as much of our own money as we please in charity; but as members of Congress we have no right so to appropriate a dollar of the public money. Some eloquent appeals have been made to us upon the ground that it is a debt due the deceased. Mr. Speaker, the deceased lived long after the close of the war; he was in office to the day of his death, and I have never heard that the government was in arrears to him. This government can owe no debts but for services rendered, and at a stipulated price. If it is a debt, how much is it? Has it been audited, and the amount due ascertained? If it is a debt, this is not the place to present it for payment, or to have its merits examined. If it is a debt, we owe more than we can ever hope to pay, for we owe the widow of every soldier who fought in the War of 1812 precisely the same amount. There is a woman in my neighborhood, the widow of as gallant a man as ever shouldered a musket. He fell in battle. She is as good in every respect as this lady, and is as poor. She is earning her daily bread by her daily labor; but

***Chairman's Statement***
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I want to thank our witnesses for being here today and I look forward to our dialogue.

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[i] Table 8.1—**OUTLAYS BY BUDGET ENFORCEMENT ACT CATEGORY: 1962–2010,** http://www.whitehouse.gov/omb/budget/fy2006/sheets/hist08z1.xls

[ii] Calculations based on OMB Object Class Analysis 2006 (includes personnel, benefits, travel, rental payments, communications, utilities, supplies, facility operation and management, etc.), http://www.whitehouse.gov/omb/budget/fy2006/pdf/objclass.pdf

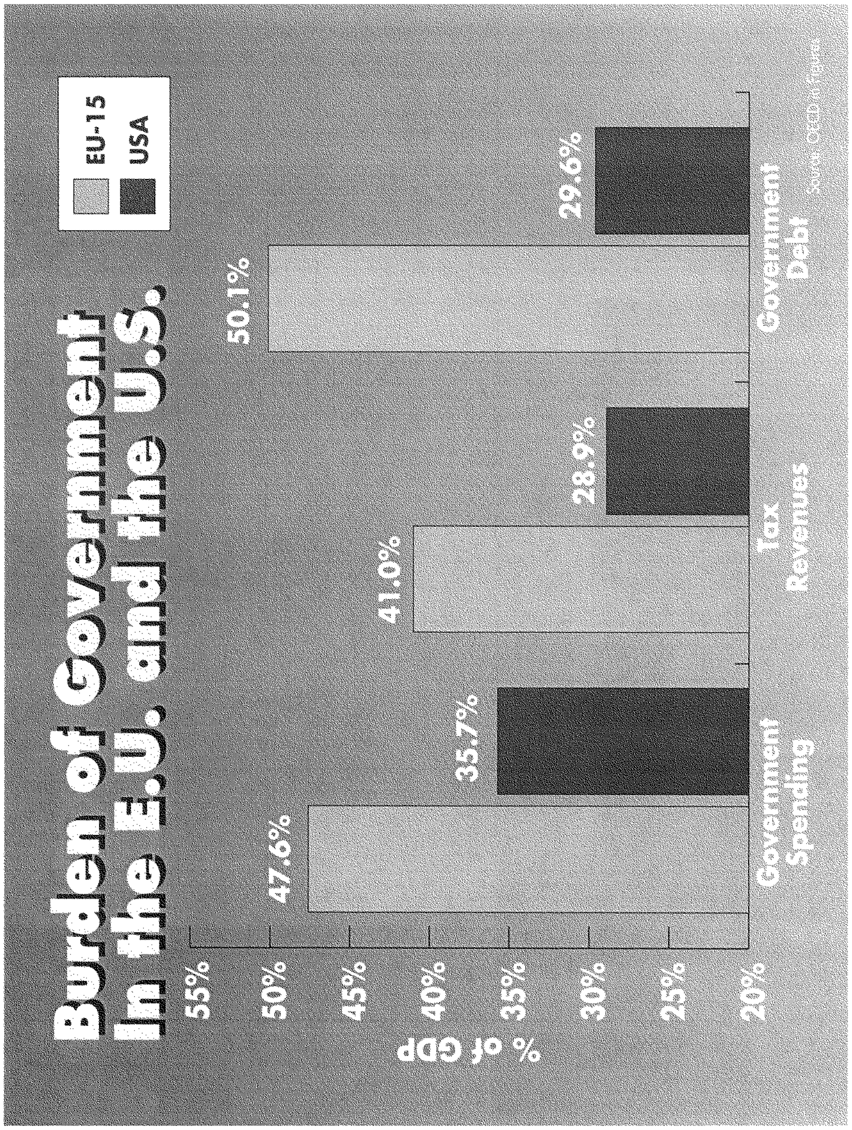
[iii] First Research Industry Profiles, http://www.firstresearch.com/IndustryAnalysis/commercialprinting.asp, (June 15, 2005.)

[iv] Index of Economic Freedom 2005, http://www.heritage.org/research/features/index/country.cfm?ID=Unitedstates, Organisation for Economic Co-operation and Development, http://www.oecd.org/country/0,3021,en_33873108_33873402_1_1_1_1_1,00.html

[v] The CIA World Fact Book 2004, http://www.odci.gov/cia/publications/factbook/geos/us.html#Econ

[vi] Index of Economic Freedom 2005, http://www.heritage.org/research/features/index/country.cfm?ID=Unitedstates, Organisation for Economic Co-operation and Development, http://www.oecd.org/country/0,3021,en_33873108_33873402_1_1_1_1_1,00.html

[vii] Government Accountability Office Baseline Extended Model, http://www.gao.gov/special.pubs/longterm/baselineextendedaugust2005.pdf


Burden of Government
In the E.U. and the U.S.
EU-15
USA
% of GDP
55%
50%
45%
40%
35%
30%
25%
20%
47.6%
35.7%
41.0%
28.9%
50.1%
29.6%
Government Spending
Tax Revenues
Government Debt
Source: OECD in Figures

**Op-Chart**

MAYA MACGUINEAS AND ALICIA CHENG

# *Closing the Hurricane Gap*

WHILE it's impossible to measure the human suffering caused by Hurricanes Katrina and Rita, it is possible to measure their effect on the nation's budget. Given our precarious fiscal situation — large budget deficits and huge imbalances in long-term entitlement programs — Congress cannot afford to blindly add billions to the already swollen deficit. In the coming years (or better yet, months) there will have to be a bipartisan effort to balance the budget for both the short and long terms. More immediately, Congress should act to make sure that the hurricanes aren't the fiscal straw that breaks the budget's back.

The first step is to hold off on any non-hurricane-related tax cuts or new spending until the full costs of the storms have been assessed. After that, Congress should build "rainy day funds" into future budgets, setting aside savings for future disasters.

Finally, Congress needs to face up to the specifics of offsetting the new costs. The following chart shows what it would take over the next five years to offset the estimated $200 billion it will take to clean up the Gulf Coast. The bulk of the offsets come from cutting spending that has already been approved by Congress. Based on the belief that any offset package should involve shared sacrifice, the reductions are spread among different areas of the budget and different regions of the country. Tax increases and cuts in entitlement programs like Medicare and Social Security are a smaller part of the package because they need to be addressed as part of larger fiscal reforms.

There are many ways to get that job done — the purpose of this exercise is to focus on the idea that budgets are about setting priorities, and that a choice to spend more in one place should be linked to a choice to spend less elsewhere.

### DEFENSE
$36.1 BILLION

- Cancel production of the V-22 Osprey aircraft ..... $6.2 billion
- Reduce the Trident submarine force to 12 from 18 and buy 48 fewer of its D-5 missiles ..... $590 million
- Reduce number of next-generation DD(X) destroyers ..... $2.5 billion
- Cancel the Robust Nuclear Earth Penetrator program ..... $8 million
- Slow development of ground-based missile defense ..... $6.2 billion
- Cancel purchase of the F/A-22 fighter ..... $15 billion
- Speed the sale of old and excess Navy vehicles ..... $120 million
- Introduce more co-payments into the military's Tricare for Life insurance program ..... $4.5 billion
- Consolidate military exchanges ..... $730 million
- Reduce military personnel in overseas headquarters positions ..... $200 million
- Reduce Defense Department administrative accounts ..... $50 million

### HURRICANE SURTAX
$25 BILLION

Progressive income surtax of up to $50 per month for five years

### CORPORATE WELFARE
$30.3 BILLION

- Eliminate tax breaks and general subsidies in energy bill for oil and gas production ..... $7.1 billion
- Reduce agriculture subsidies ..... $11.1 billion
- Eliminate the Export-Import Bank and Overseas Private Investment Corporation ..... $620 million
- Hold additional wireless spectrum auction ..... $9 billion
- Eliminate the International Trade Administration's trade promotion activities ..... $2 billion
- Eliminate the Commerce Department's advanced technology program ..... $500 million

### CONSUMER PRICE INDEX
$50 BILLION

Update the inflation estimate used to calculate cost of living adjustments for government programs and taxes

### POORLY DIRECTED PROGRAMS
$5.5 BILLION

- Phase out subsidies for federal flood insurance ..... $220 million
- Drop wealthier communities from community development block grants ..... $2.5 billion
- Restrict homeland security first-responder grants to larger, at-risk communities ..... $2.4 billion
- Rescind Title I, No Child Left Behind and Individuals With Disabilities Education Act money that would have gone to education programs in the hurricane region ..... $400 million

### SPACE EXPLORATION
$10.2 BILLION

Cancel the crew exploration vehicle and lunar and Mars exploration programs

### MEDICARE AND PRESCRIPTION DRUGS
$13.7 BILLION

- Apply a means test to the Medicare prescription plan premium ..... $3.8 billion
- Reduce financing for the Medicare Advantage Stabilization Fund, which gives H.M.O.'s inducements to participate in Medicare ..... $2.9 billion
- Change the formula that updates hospital inpatient operating costs under Medicare ..... $7 billion

**TOTAL SAVINGS**
**$200 BILLION**

### GENERAL PORK
$20 BILLION

*Place a one-year moratorium on new earmarks in annual appropriations bills. Some earmarks approved last year include:*

- Curriculum for mariachi music, Clark County School District, Nevada ..... $25,000
- Stabilization of bathhouses for re-use, Hot Springs, Ark. ..... $25,000
- Punxsutawney Weather Museum in Pennsylvania (hometown of groundhog that supposedly predicts length of winter) ..... $100,000
- Country Music Hall of Fame, Nashville, Tenn. ..... $250,000
- Paper Industry International Hall of Fame, Appleton, Wis. ..... $75,000
- Demonstration project to transport naturally chilled water from Lake Ontario to Lake Onondaga, N.Y. ..... $1.5 million
- Therapeutic horseback riding program at the Lady B Ranch, California ..... $150,000
- Animal waste management research laboratory, Bowling Green, Ky. ..... $2.3 million
- Project to protect sunflowers from birds, North Dakota ..... $335,000
- Study of catfish genomes, Auburn University, Alabama ..... $225,000
- Marine turtle program ..... $1.5 million
- Kincaid Park Soccer and Nordic Ski Center, Anchorage ..... $500,000
- High Falls Film Festival, Rochester ..... $100,000
- Missouri Pork Producers Federation to convert animal feces into biomass energy ..... $1 million

### TRANSPORTATION PORK
$9.2 BILLION

*The $286 billion transportation package signed by President Bush in August has plenty of candidates for trimming:*

- "Infrastructure Awareness Program," a documentary "about infrastructure that demonstrates advancements in Alaska" ..... $3 million
- High Knob Horse Trails, Virginia ..... $600,000
- Landscaping enhancements along the Ronald Reagan Freeway, Ventura County, Calif. ..... $2.3 million
- National Infantry Museum transportation network, Columbus, Ga. ..... $2.4 million
- Transportation enhancements, Children's Museum of Los Angeles ..... $960,000
- Blue Ridge Music Center, Connecticut ..... $1.6 million
- Deer avoidance system in Pennsylvania and New York ..... $200,000
- Cultural and interpretative center, Richland, Wash. ..... $1.3 million
- Henry Ford Museum, Dearborn, Mich. ..... $1.2 million
- Waterfront walkway, Oswego, N.Y. ..... $1 million
- Uptown jogging, bicycle and trolley trail, Columbus, Ga. ..... $400,000
- Oklahoma transportation center to study motorcycle accident investigation methodology ..... $1.4 million
- Wood-composite products demonstration project, University of Maine ..... $1 million
- "Bridge to Nowhere" joining Gravina Island (population 50) to Ketchikan, Alaska ..... $223 million

*Sources: Congressional Budget Office; Congressional Joint Tax Committee; Government Accountability Office; Taxpayers for Common Sense; Citizens Against Government Waste; Republican Study Committee; Web site of Senator John McCain*

Senator COBURN. I want to thank our witnesses for being here today and I look forward to your dialogue.

I would now like to recognize my Ranking Member and friend, Senator Carper.

## OPENING STATEMENT OF SENATOR CARPER

Senator CARPER. Thanks, Mr. Chairman. It is great to be here with you and it is also a special privilege to be here with our former colleague, Charlie Stenholm.

Congressman Stenholm and I had the pleasure of working together along with Larry Craig when we were all in the House to draft the Balanced Budget Amendment to the Constitution, not one that mandated a balanced budget every year but one that said, starting at a date certain, the President had to propose a balanced budget and to say that the Congress could vote to unbalance the budget, but you would need a majority to do that, three-fifths vote, and a super-majority to raise the debt ceiling. I think we got within about a dozen votes of getting that through the House of Representatives.

Later, Congressman Stenholm and I worked on passing the first, I call it statutory line item veto bill that enhanced the recision powers of the President and served as almost a test drive, if you will, for line item veto powers for the President, the first one, I think, that ever passed the House. It didn't make muster here in the Senate, or at least not that year, but I know he has continued to be a champion for that proposal and all kinds of fiscally responsible measures.

I thank our other witnesses for their presence here and look forward to each of your testimonies.

Mr. Chairman, I am grateful that we are having this hearing and thank you for chairing it.

We recently got some good news about our Federal budget deficit. About 2 weeks ago, we learned that the Federal budget deficit for 2005 was only about $319 billion—I put that "only" in quotes—rather than the $400-plus billion that some had expected at the beginning of the last budget cycle. That was the good news, only $319 billion. The bad news is that a $319 billion budget deficit actually passes for good news in the environment in which we are operating today.

This year's budget deficit for 2006 may well be even larger, some say as much as $400 billion, and beyond next year, the story will be much the same, larger budget deficits adding to a growing national debt, particularly as guys like me, baby boomers, as our generation moves toward retirement and puts a real stress on spending in this country.

How did the Federal budget end up in a ditch just when a little more than 4 years ago, we enjoyed budget surpluses for as far as the eye could see. I think it is really fairly simple. In terms of total government outlays under the current Administration, we have spent more, I think, than any administration, any Congress in the last 35 years, at least in the time I have been following these developments. At the same time, the Bush Administration is pushing billions of dollars in tax cuts, some unwise, thus reducing our revenue base. Today, it is down to about 17.5 percent of GDP, which I think is the lowest since a bunch of us have been alive.

The bottom line is that we are spending more than we are taking in, and as any family would tell us, that is a recipe for a budget that is out of balance, whether it is for a Federal Government or for a family.

During my years in public service, I have always tried to reconcile my position on fiscal issues with the basic tenet that if something is worth doing, it is worth paying for. Unfortunately, neither the Bush Administration nor this Congress is following that principle. Instead, we are doing a lot and paying for too little of it. We are fighting wars today, as we know, in Afghanistan and Iraq. We are dealing with the aftermaths of Hurricane Katrina and Rita and soon Hurricane Wilma. We are implementing a new drug benefit for senior citizens and paying for recent tax cuts with money that we are borrowing from countries like China, like Japan, like South Korea, just to mention a few. In a sense, the world is paying our bills.

This can't last. We have to someday begin to pay our creditors back. If we don't change our fiscal ways, it is likely that our children and grandchildren will be the ones who are going to be asked to do that paying back.

Getting our budget back on a path to balance will require this Administration and Congress to make tough decisions, which we have been reluctant to do at least to this point in time. But before we can make—and really, not just difficult decisions, but really calling on the American people and ourselves to do some shared sacrificing.

Before we can make those decisions, it is essential that the White House and the Congress first admit to the size and scope of our budget problems. Once that has been done, it will be clear that we can't fix our budget problems by focusing either only on spending or only on the tax side of the ledger. Everything will have to be on the table, our tax policies, discretionary spending, defense spending as well as domestic spending, mandatory spending, and, I think, the budget process itself.

Until that time, Democrats and Republicans should come together and do everything in our collective power to ensure that the problem that we have inherited, in some cases made, is not made worse.

My friends, I think we are in a hole. Some of you remember the former Chancellor of the Exchequer, a guy named Dennis Healey. He used to talk about the theory of holes, and the theory of holes, as you may recall, is when you find yourself in a hole, stop digging. And to that end, I think we should get serious about budget enforcement. We should reinstate the pay-as-you-go rules that require spending increases and tax cuts to be paid for by either cutting spending or raising revenues. And I am confident that both sides of the aisle can also agree to once again put in place caps on discretionary spending.

Mr. Chairman, thank you again for calling this hearing. I am delighted to be here sitting next to you and especially pleased to welcome our witnesses, including our old colleague here, Charlie Stenholm.

Senator COBURN. Thank you, Senator Carper.

Let me introduce our witnesses, if I may. The first gentleman, I have known since 1994, who has become a close friend of mine. I tried to get him to live with me, but he is so tight, he lives in his office, and so he wouldn't share the cost of that. It is Congressman John Shadegg. He represents the Third District of Arizona. He got up very early in the morning to get here from Arizona to be here for this hearing and I want to tell him personally how much I appreciate him doing that. He is the author of the Enumerated Powers Act in the House. As a member of the Republican Study Committee, he currently chairs the House Republican Policy Committee.

Next is Congressman Charlie Stenholm, Government Affairs Advisor for Olsson, Frank and Weeda, P.C. He represented the 17th District of Texas for 26 years in the U.S. House of Representatives. He was Chair of the Blue Dog Coalition and a man of immense integrity and honor that I have felt fortunate to serve with.

Next is Dr. Roger Pilon, Vice President for Legal Affairs and founder and Director of the Center for Constitutional Studies at the Cato Institute. He founded the Center for Constitutional Studies at the Cato Institute in 1989 and he holds the B. Kenneth Simon Chair in Consitutional Studies. Prior to joining Cato, he held five senior posts in the Reagan Administration, at the Office of Personnel Management, the State Department, and the Justice Department.

And last but not least is Dr. Daniel J. Mitchell, McKenna Senior Fellow in Political Economy at The Heritage Foundation. He is the chief expert on tax policy and economy at Heritage. He is a former Finance Committee economist under Senator Bob Packwood. He is also an expert on economies of member countries of the European Union.

I welcome each of you. We will start with Congressman Shadegg. There is not going to be a time limit on your testimony. We have read your testimony. We appreciate it. Feel free to expand on that and then we will have some questions for you, if that is OK with the Ranking Member.

Congressman Shadegg.

## TESTIMONY OF HON. JOHN SHADEGG,[1] A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARIZONA

Mr. SHADEGG. Thank you, Senator. I appreciate the opportunity to be here to discuss both the Tenth Amendment and the legislation I have in the House, the Enumerated Powers Act.

I understand that before I arrived—I arrived as soon as I landed—you had already read parts of the story of Davy Crockett and his floor speech and his experience out with his constituents who taught him a lesson that I think has been lost on Members of Congress and, indeed, lost on the public in America, and that is a great story. It is incorporated in its full length in a "Dear Colleague" that I have circulated for years in the House in my efforts to secure support for the Enumerated Powers Act.

[1] The prepared statement of Mr. Shadegg appears in the Appendix on page 48.

I also note that you have up here some quotes from Thomas Jefferson and the language of the Tenth Amendment, all of which are in my testimony. I am going to summarize some of my testimony rather than read all of it and just hit the key points. I would like, of course, the entire testimony be included in the record.

As you have noted by putting it up, the Tenth Amendment provides that the powers not delegated to the United States by the Constitution nor prohibited by it to the States are reserved to the States respectively or to the people. That is language that is, as I indicated, I think lost on most Americans. In other words, the National Government cannot expand its legislative authority into areas reserved to the States or to the people.

As the final amendment of the Bill of Rights, the Tenth Amendment makes it clear that the Constitution established a Federal Government of delegated, enumerated, specific powers and thus created a limited government. The notion today that the Federal Government can do anything people want it to do is simply wrong.

As a result of that, every Congress since the 104th, I have introduced, as you noted, the Enumerated Powers Act. It is a simple piece of legislation which perhaps by its simplicity scares Members of Congress too much. It simply says that every bill introduced by a Member of Congress or a Member of the Senate into the U.S. House or U.S. Senate would have to contain a statement citing the specific enumerated power granted to Congress to legislate in that particular area.

Quite frankly, Article I, Section 8 sets forth those enumerated powers. There are 18 set forth. In trying to secure passage of the legislation, I am often asked by people who review it, “Well, Congressman, how would we justify,” and then they cite some law already in place, and my answer is typically, simply because we have been doing things wrong, in violation of oath of office, for that matter, for years, doesn’t mean we should go on doing them.

A lot of people think the Tenth Amendment is a dead letter. I would remind this Subcommittee, and I know my colleagues here at the panel already know, as recently as 1996, in *United States v. Lopez,* the U.S. Supreme Court ruled that Congress did not have the authority to pass certain legislation. The legislation specifically under review at the time was the gun-free schools legislation. Although many can argue that such zones may be a good idea, what the Supreme Court concluded was that Congress simply lacked the power under the U.S. Constitution to mandate gun-free school zones. It determined that even the Interstate Commerce Clause did not give it that authority or that power. As you know, the Interstate Commerce Clause is cited quite often as a rationale for much of what we pass.

In his, I think, famous book, the conscience of the conservatives, Senator Goldwater, explained what he felt his duties were. One of them was, and I cite this in my testimony, “I will not attempt to discover whether legislation is needed before I have first determined whether it is constitutionally permissible.”

I think *United States v. Lopez* reminds us that is an ongoing obligation. Justice Kennedy concurred in the opinion and he wrote, “It would be mistaken and mischievous for the political branches to forget that the sworn obligation to preserve and protect the Constitution in maintaining the Federal balance, that is, respect for the powers reserved to the States and for the powers reserved to the people, is theirs, that is, is the legislative branch's, in the first and primary instance." That is to say, what Kennedy was saying to us is we have an obligation as a legislative body to fulfill our oaths and to honor the Constitution and to honor the Tenth Amendment and its prohibition.

Simply put, when the Founding Fathers wrote our Constitution, they created a National Government with far-reaching powers, but with constitutionally limited powers, and they believed that granting specific rather than general legislative authority to the Federal Government would be one of the ways to control the mechanisms and to protect our freedom.

I think it is worth noting that when the Constitution was written, there had been a very extensive debate about what should the role of the Federal Government be, and indeed, the Founding Fathers spent a lot of time writing out in detail what that role should be. Today, unfortunately, we have totally forgotten it.

For the first 150 years of our history, from 1787 to 1937, the National Government was itself, the Congress was itself the bulwark against an expansive Federal Government legislating in all kinds of areas that it felt like. Unfortunately, that restraint demonstrated by those early Congresses has all but been totally abandoned in this century and in the immediately preceding century. Beginning with the New Deal era, modern Congresses have displayed a willingness to pass any kind of law that they feel like.

I think it is worth nothing that virtually all of these laws, whether they are civil rights or labor or environmental, you name it, are always, indeed, I would agree in every single instance they are well intentioned. But the point is that simply from a constitutional perspective, Congress does not possess the authority to enact them. Indeed, that authority is specifically reserved for the States or perhaps to the people themselves.

Nonetheless, we as a government have ignored the Constitution and expanded the authority of the Federal Government into every aspect of human conduct. The size and scope of our National Government has exploded over the past seven decades, as was noted here in the opening remarks, and many even doubt whether there is any life in the portion of the Constitution which restricts our powers. Yet the belief that the central government should have only limited powers remains alive in the hearts of many Americans who believe that people, not government programs, hold the answer to our Nation's problems.

I would note that I think right now, when we are confronted with a Federal Government out of control and we are confronted with spending at a level unimagined in even just recent years, just recently ago, Mr. Chairman, as when you and I were elected to the House, in the wake of Hurricane Katrina and at a time when Federal spending has ballooned to an unsustainable level, I think this is a perfect time to hold this hearing. It is a perfect time to cut back on some of the spending that occurs in Washington on programs wrongfully undertaken by the Federal Government, clearly outside the scope of our constitutional authority, and I would urge that we should institute a system something like that contemplated by the Enumerated Powers Act that simply forces Congress to reflect on whether or not legislation which is proposed, in fact, fits within our powers.

Today, many Americans, and I think you can see this particularly in the wake of the hurricanes, not only expect the Federal Government to solve all their problems, it has never even occurred to them that the Federal Government does not have under our Constitution the authority to do that. I think one of the most important things this Congress could do would be to honor and abide by the principles embodied in the Constitution, no more, no less, and to respect the Tenth Amendment as it was written and to respect the division of power between the Federal Government, the States, and the people.

It seems sad to me that many of our governors don't exercise or demand that we exercise their authority or ours. They could be pointing today to the Tenth Amendment and to the Enumerated Powers Clause of the Constitution and saying the Federal Government can't legislate in these areas. Instead, what they are doing is demanding that the Federal Government spend more and more and more and legislate in all those areas.

I would conclude, Mr. Chairman, you have put up a quote from Thomas Jefferson. I want to conclude with one—I concluded my written testimony with a quote from Senator Goldwater. I will conclude my testimony here with one from James Madison, the Father of the Constitution. Often, the provision that is cited by those who want to justify Congress legislating in any area it feels like is, of course, the General Welfare Clause. James Madison, the Father of the Constitution, said, "If Congress can do whatever in their discretion can be done by money," the point that was made here, "and will promote the general welfare, then the government is no longer a limited one." Thomas Jefferson went on to say, "Congress does not possess unlimited powers to provide for the general welfare, but we are restrained by those specifically enumerated."

It seems to me that if the Framers intended the General Welfare Clause to have the interpretation that current Congresses put on it, they could have spared themselves considerable grief and contentiousness in that hot, humid summer in Philadelphia of 1787 and they could simply have written, "Congress shall promote the general welfare." They did not do that. They intended a different result, and the consequences, I think, are damaging our Nation today.

I would be happy to answer any questions.

Senator COBURN. Thank you, Congressman Shadegg. Congressman Stenholm.

**TESTIMONY OF HON. CHARLIE STENHOLM,[1] GOVERNMENT AFFAIRS ADVISOR, OLSSON, FRANK AND WEEDA, P.C., AND FORMER REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS**

Mr. STENHOLM. Thank you, Mr. Chairman. Mr. Chairman and Senator Carper, it is indeed a pleasure for me to be here and thank you for affording me the opportunity to testify before you today on

[1] The prepared statement of Mr. Stenholm appears in the Appendix on page 55.

the subject of which you have asked the question asked by this hearing, how can Congress justify spending billions of taxpayer dollars on wasteful and ineffective programs when we are a Nation at war, recovering from the worst natural disaster in our history, already stretched thin by record non-military spending?

It virtually answers itself. We can't. The fact that such a question even has to be asked at a Congressional hearing underscores just how far we have strayed from the path of fiscal responsibility.

It should be equally obvious that we can't keep cutting our revenues as we face higher expenses for war and disasters. As a longtime advocate of pay-as-you-go budgeting, it is heartening to hear talk again about offsetting the costs of legislation to prevent the deficit from increasing. Unfortunately, the leadership in Congress didn't rediscover the common sense principle of pay-as-you-go until after enacting legislation that added several trillion dollars to our Nation's debt. Even now, the leadership continues to apply the principle selectively.

I applaud the efforts that many of you have made to find offsets for the cost of disaster relief in the Gulf Coast. However, to me, it is far more important that Congress offset the cost of legislation that will have a permanent impact on the long-term budget outlook. Focusing on offsetting the one-time temporary cost of disaster relief while ignoring the cost of legislation that will permanently increase the deficit by a much greater amount over the long term makes no sense.

I would like to believe that the leadership in Congress has undergone a conversion on the road to Damascus in fiscal policy, but the refusal to reconsider legislation enacted over the last several years which has led to our current deficit situation and the insistence on moving forward with tax cuts and other legislation that would increase the deficit casts doubt on the seriousness of their newfound concern for the deficit.

It is true, when we start talking about the deficit, it is true that our Nation has faced unexpected emergencies that have contributed to the deficit, but that is not an excuse for running deficits. Many of us warned that the anticipated budget surpluses just a few years ago were only projections and that it was dangerous to make commitments using all of the projected surpluses without leaving any room for error. We warned that if the projections didn't turn out exactly as hoped, we would return to deficits. We should have set aside some of the projected surplus as a cushion to prepare for unanticipated costs.

Defenders of our current economic and fiscal policies have argued that deficits don't matter. You notice that I said "we" because I was part of those votes up until December of last year. The reality is, though, that deficits do matter. It has been mind-boggling to me to hear some of my conservative friends, that when the shoe was on the other foot, we were talking about how bad the deficits were, to suddenly now say deficits don't matter anymore. The reality to me is that deficits do matter, both for our economic security today as well as the future we leave for our children and grandchildren.

Our increased reliance on foreign capital to finance our deficits places our economic security at the mercy of global bankers and foreign governments. Large deficits financed by borrowing from foreign investors are also a major factor contributing to the trade deficits which we are now exporting jobs at a very rapid rate.

We need to keep the value of the dollar high in order to attract the foreign capital we need to finance our debt. If the value of the dollar declines, U.S. bonds will be less valuable to foreign investors, but the strong dollar we need to help Treasury finance our budget deficit hurts our business by making U.S. exports more expensive. Round and round we go.

Deficits do matter. Our current borrow-and-spend policies, to me, are worse than the tax-and-spend policies of the older days. When you tax and spend, you are politically accountable, and I love the sign up here talking about accountability. When you vote to tax people to do, as my colleague Mr. Shadegg says here, when you vote to do things that some decree as being unconstitutional, there is accountability and you pay for that at the ballot box, or at least you should. But when you borrow and spend, there is no accountability.

My three grandchildren, my three grandsons, don't have a vote on what I did when I was in the Congress or what you will do this year in the Congress and that is where the accountability is. Our grandchildren do not have a vote. That is why it is so easy for us to say today we can fight two wars, fund homeland security, fight the war on terrorism, rebuild the Gulf Coast, and keep cutting our taxes, because we are going to send the bill to our grandchildren.

It is neither fiscally responsible nor politically viable to make cutbacks in some areas of the budget in the name of deficit reduction while exempting other areas. If we really want to get serious, everything has to be on the table, everything. Otherwise, you will never get there. It is neither fiscally responsible nor politically viable to make cutbacks in some areas while exempting others. It will take everyone pulling to get the wagon out of the ditch. We won't be able to get it out if some people are riding.

The first step in bringing the deficit under control is to stop digging the hole deeper. I used to give that quote. I am glad to know who should have the credit for that. I used to say it was either Confucius or Garfield, but——

Senator CARPER. Congressman, I used to attribute it to you. I found out it was Dennis Healey.

Mr. STENHOLM. Well, that is dangerous around here.

Rhetoric about controlling the deficit by offsetting increased spending doesn't have much credibility when Congress continues to go forward with plans to add additional tax cuts.

Now, there will be those that argue that—and we have now enacted three tax cuts based on the theory that tax cuts will stimulate the economy, and some of them do, no question about that, and pay for themselves as a result of economic growth. There is a big question about that. As one who voted for the Reagan tax cuts in 1981, I also remember the tax increases of 1982, 1983, 1984, 1985, and 1986 in which we adjusted, in a bipartisan way, we adjusted for the economy to avoid building the deficits to alarming heights. Today, we don't worry about $300 billion, $400 billion deficits.

Each time, advocates of the tax cuts dismissed warnings about the impact on the deficit, yet the deficit continued to grow. Although some advocates of tax cuts have claimed that recent reports showing higher than expected revenue collection last year is evidence that the fiscal policies of the last 5 years are working, the reality is that the recent increase in revenues just partially begin to restore the decline in revenues over the last several years.

There are many reasons that actual revenues have been much lower than Congress and the Administration projected when the tax cuts were enacted, but clearly, those tax cuts have not paid for themselves and have been granted with borrowed money.

So my first point is, you have got to put everything on the table. Any serious effort to restore fiscal deficits should begin with reinstating the pay-as-you-go budget, already mentioned by Mr. Carper and by you, Mr. Chairman. It is a darn good idea. It is very simple. If you are going to spend for anything, you have got to find someplace to cut. But why we have selectively stopped doing what we did successfully in 1990 and 1997 in which everything was on the table, including if you are going to cut taxes, you have got to cut spending first or find other revenues to replace that so the deficit does not grow large.

For some reason, and I would say, with all due respect to my republican friends, that if you are sincere in what you say about controlling spending, you should not have a problem with reinstating pay-as-you-go for taxes as well as spending because it would force Congress to actually cut spending to accompany the tax cuts instead of just promising to cut spending in the future. That has been the weakness that we have gotten into.

One small step that would help restore a small measure of fiscal discipline is enactment of expedited recision. Senator Carper, you and I worked on that. Dr. Coburn, you have been the champion lately of that same process. It makes good sense. We went through this with line item veto and there were a lot of folks that were saying we ought to give the President line item veto. Some of us had a little problem with that because of the Constitution, of granting an individual, in this case the President, something that was not enumerated in the Constitution. And sure enough, we found out it could not be done. The Supreme Court ruled against it. But modified line item veto makes good sense.

Dr. Coburn, last week when you attempted to extract some spending from the budget, it would sure be nice if the President of the United States could go in and either say, those spending items that you were trying to extract should be in the budget because they are necessary spending or they should not, and as I have always said, you could take my pork, that which I put into the budget, and President, you can veto it. All I ask is a chance to have 50 percent plus one of my colleagues to agree with me or with you.

Therefore, we get into the problem that Mr. Shadegg is talking about, what is enumerated in the Constitution and what is not. If my programs are not enumerated, i.e., by 50 percent plus one—a little slightly different take than what Mr. Shadegg is talking about—I am perfectly willing. I think it makes good sense. Expedited recision would bring greater accountability, all of those things up there, and I hope the Senate, you in a bipartisan way, will look at implementing a modified recision order.

Another tool that Congress should consider to eliminate low-priority spending is sunset legislation to provide for regular review of the efficacy of various programs. Here, if our committees, and I will speak for the Agriculture Committee in the House, we need to spend more time in oversight. One of the few members on the House side that has done anything along this line is Joe Barton of Texas in saying that many of the programs in the energy and commerce and the health area, we passed them and nothing ever happens because we don't look at it. We ought to spend a little more time in that and sunsetting, and one good way to do it is to have every program stop every 10 years unless it is reauthorized. That is not a bad idea.

Moving on real quickly, I think we ought to—or recommend to you, I should say, to seriously look at changing the way the CPI is calculated. Today, if we can debate, and we do debate various credibility of any government program, but having an automatic cost-of-living adjustment that is not accurate makes limited amounts of sense, and there are several ideas out there that can be extremely helpful in making sure that the CPI is calculated, different views, different ideas, but I recommend you take a look at it.

I would hope that this would be the year that Congress and the President will take a look at, Mr. Chairman, what you mentioned in your opening remarks, and that is the unfunded liabilities of the many programs—Social Security, Medicare, Medicaid. But it wasn't to be. We did not have the leadership or the followership in a bipartisan way to deal with a program that must be dealt with, no question about it.

When I first started being concerned about that, I didn't have any grandchildren and 2011 was a long time away. That is when the baby boomers are going to begin to reach age 65. Well, 2011 is not very long away and every day we wait to fix Social Security, and then everybody will chuckle and say that was the easy one. Medicare is going to be the tough one, Medicaid, in this. But we postponed that for another year.

In conclusion, Mr. Chairman, I have attached an op-ed chart published in the New York Times by Maya MacGuineas. I also have the privilege of now serving on the Board of the Committee for Responsible Budget. You mentioned Pete Peterson's book. I have read it twice. I enjoy serving with him and many of the views that we have, have come from him. I also serve on the Board of the Concord Coalition, which is Pete Peterson—I got mixed up there, but some good ideas. The Center for Budget and Policy Priorities, a little more liberal group, but when you put all three of those, and I recommend that you or your staffs take a look at how much agreement we have on how you could truly do something about the budget deficit.

Just today, and as I said, I am speaking for myself, but a press release issued by the Committee for Responsible Budget urges Congress to proceed with the spending cuts while holding off on the tax cuts. I join in that recommendation. We only disagree with some of the individual items suggested, but if we are ever going to get a solution, we are going to have to find a way to work together. You can have the greatest idea since sliced bread, but as a member of the House, unless I could find 217 to agree with me and then

51 Senators, it was never going to happen or you were never going to keep it from happening.

One of the happiest days of my life was seeing the balanced budget constitutional amendment pass in the House of Representatives. One of the saddest was watching it be defeated in this body by one vote. If we had passed that constitutional restraint, we would not have near the severe budget problems that we have today. Thank you, Mr. Chairman.

Senator COBURN. Thank you, Congressman Stenholm. Dr. Pilon.

## TESTIMONY OF ROGER PILON,[1] VICE PRESIDENT FOR LEGAL AFFAIRS, B. KENNETH SIMON CHAIR IN CONSTITUTIONAL STUDIES, AND DIRECTOR, CENTER FOR CONSTITUTIONAL STUDIES, CATO INSTITUTE

Mr. PILON. Thank you very much, Mr. Chairman. Thank you for inviting me here to testify, and thank you especially for calling these hearings on a subject that is too rarely considered in this body as well as the body across the way, namely, what is the constitutional authority for so much of what Congress is doing. I am here to take a very serious position, namely that most of what this Congress does is beyond the authority of the Congress to do because it is done without constitutional authority.

A decade ago, I had the pleasure of working with Congressman Shadegg over in the radical 104th Congress, his first year in Congress, with the Constitutional Caucus that was created at that time. It was a heady time when we thought we might be able to do something about this. Unfortunately, it did not come to pass, but I will say a little more about that in a few minutes.

I appreciate the fact that you have lifted the normal time restraint. However, I want to assure you I will not read the 17 pages of single-spaced testimony that I have prepared. I would ask, however, that it be included in the record.

Senator COBURN. Thank you, and without objection, it will. All testimony will be included in the record.

Mr. PILON. All right. Good. Now, the main point that I drew out of that testimony was the point about constitutional legitimacy and that is what I want to focus upon primarily in my remarks. Congressman Shadegg has covered a good deal of what I included in my testimony. I will just fill in interstitially some of the points surrounding that.

I wanted to focus on the Constitution's theory of legitimacy and then raise three questions that arise from the fact that so much of what Congress does today is done without constitutional authority, namely how did we get to this state of affairs; second, what are the implications of it; and third, what is to be done about it?

This issue of legitimacy is, unfortunately, too little understood not only in this body, but in the country at large, although I think, Mr. Chairman, that you are absolutely right that out there in the country, there are a lot of people who have at least an intuitive understanding that Congress is acting way beyond its constitutional authority.

[1] The prepared statement of Mr. Pilon appears in the Appendix on page 63.

After all, Madison said in Federalist 45, when he was trying to assure a Nation that was concerned that the new Constitution the Philadelphia Convention had drafted was giving too much power to the National Government that the powers of the Federal Government were to be few and defined. I don't think anyone in this room thinks that the powers of the Federal Government today are few and defined, and so the question is how did we get from there to here?

The theory of legitimacy starts with the Preamble. We, the people, for the purposes listed, do ordain and establish this Constitution. Therefore, all power starts with the people. The theory of the Constitution is really quite simple. They give the government certain powers. They retain the rest themselves, either giving them to the State or retaining them, never having given them to either level of government.

The first sentence of Article I says, all legislative power herein granted shall be vested in the Congress. By implication, not all power was herein granted. Look at Article I, Section 8, and you will find 18 powers that were granted to Congress: The power to tax, the first power; the power to borrow, the second power; the power to regulate international and interstate commerce, the third power; and so on, culminating with the necessary and proper clause which provides Congress with the means to carry out those other powers.

Now, that theory of legitimacy, namely that the government has only those powers we have given it, is one that we lived under pretty much for 150 years, as Congressman Shadegg said, and we see examples of it during that period. You drew upon the little volume by Charles Warren, Congress as Santa Claus, a title that captures volumes about what is going on today. And in there, you find a storehouse of examples of Congress, the executive, and the courts resisting the inevitable impulse towards ever-larger government.

Remember, Jefferson said it is the tendency of government to grow and liberty to yield, and we have seen that right from the beginning. Hamilton's report on manufacturers in 1791 was a national industrial policy that the Congress fortunately shelved. In 1794, Madison was based with a bill for the appropriation of $15,000 for French refugees who had fled from an insurrection in San Domingo to Baltimore and Philadelphia. He rose on the floor of the House to say, I cannot undertake to lay my finger on that passage of the Constitution that authorizes us to expend the money of the taxpayers on this humanitarian activity. Two years later, his colleague, Giles from Virginia, faced with a bill appropriating funds for people suffering from a fire in Savannah said our duty is to uphold the Constitution and our oath not to engage in these eleemosynary activities.

And so it went largely through the 19th Century. Oh, there were efforts, to be sure, but they were resisted. In fact, what we see as late as 1887, 100 years after the Constitution was written, was a bill appropriating for the relief of farmers in Texas, excuse me, Congressman Stenholm, for the relief of farmers there suffering from a drought, to buy them seeds. It did make its way out of Congress but President Cleveland vetoed it on the ground that I can find no authorization for this expenditure in the Constitution.

And so what we have here is a pattern. They were rejecting these programs and these proposals and these bills not on budgetary grounds, but on constitutional grounds, on the ground that we have no authority. And so the pattern we see during these first years, largely for 100 or more years, was this: Bills rarely got out of Congress, and when they did, Presidents would veto them, and when they didn't, the court would stand to thwart these efforts to expand government. And so the pattern largely held, the system of checks and balances largely held because Congress, the President, and the courts took the Constitution seriously. They asked, do we have authority under the Constitution to engage in this particular action?

Contrast that with the Gun–Free School Zones Act that Congressman Shadegg raised a few minutes ago. That was passed in 1990 by Congress without Congress so much as even citing its authority under the Constitution for the Act. During oral argument in the Supreme Court, the Solicitor General had to bootstrap the authority into his argument by pointing to the Commerce Clause. When that came up from the Fifth Circuit in Texas, the Fifth Circuit had found it constitutional because exceeding Congress' authority. For the first time in nearly 60 years, this had been said by a court, referencing the Commerce Clause.

When it did, we at the Cato Institute commissioned a paper by a professor at the University of Texas which we entitled, "Kids, Guns, and the Commerce Clause: Is the Court Ready for Constitutional Government?" We thought that title might attract their attention. Well, the official wisdom in Washington said that would be reversed nine-to-nothing. The conventional wisdom was set back on its heels when the Court, five-to-four, upheld the Fifth Circuit and found the statute unconstitutional.

And so what did Congress do? It repassed the statute, citing the Commerce Clause this time and including a jurisdictional element in the hope that it might be found constitutional on the second goaround. So much for the respect for the Constitution that the Congress is showing so often today.

Now, when did all of this change? It changed, as Congressman Shadegg said, during the New Deal. But the precursor of the New Deal was the Progressive Era and it is important to focus upon that because it is at that time that the climate of ideas fundamentally changed. Whereas the founding generation thought of government as a necessary evil, the progressives thought of government as an engine of good, an instrument through which to solve all manner of social and economic problems. Borrowing from German schools of good government, from British utilitarianism, which had replaced the natural rights theory on which the Constitution rested, they simply wanted to have program after program addressing the problems of society. It was to be better living through bigger government, if I may paraphrase the DuPont slogan from a few years ago.

Well, of course, the pesky Constitutions to dethwart that effort and the willingness of the courts to enforce it up until the New Deal and the shift in focus by the progressives from the State level to the Federal level, at which time one program after another from Roosevelt was found to be unconstitutional.

After the landslide 1936 election, Roosevelt unveiled his notorious Court-packing scheme, his threat to pack the Court with six additional members. Not even Congress would go along with that. Nevertheless, there was the famous switch in time that saved nine. The Court got the message and it began rewriting the Constitution without benefit of constitutional amendment and it did it in two main steps.

In 1937, it eviscerated the Doctrine of Enumerated Powers, the very centerpiece of the Constitution, the very foundation of legitimacy. And in 1938, it bifurcated the Bill of Rights and gave us a bifurcated theory of judicial review.

In the 1937 effort to eviscerate the Doctrine of Enumerated Powers, it took two clauses, the General Welfare Clause, so-called, and the Commerce Clause, turned them on their head, turned them into instruments for expanding government power. They effectively unleashed the modern redistributive and regulatory State.

And in 1938, because the Bill of Rights was still standing, you could invoke your rights against this overweening power, they bifurcated the Bill of Rights to distinguish fundamental from nonfundamental rights, developed two levels of judicial review, gave us the incredibly convoluted constitutional jurisprudence that we have today which makes the Constitution all but inscrutable to the layman.

Now, in the 1937 evisceration of the Doctrine of Enumerated Powers, I want to point to the General Welfare Clause, so-called, because that is primarily at issue before these hearings. The General Welfare Clause, there is no such clause in the Constitution. It is, in fact, a phrase in the taxing power. The Congress has, in the first of its enumerated powers, the power to tax. The second, the power to borrow.

The idea that there is a General Welfare Clause comes from the debate between Hamilton and Madison early on arising out of the report on manufacturers that Hamilton gave to Congress in 1791. In 1936, in the *Butler* case, the Court entertained that debate, came down on Hamilton's side in dicta. In 1937, in the *Social Security* case, they elevated the dicta to the holding of the case. And so that is where we have this so-called General Welfare Clause to wrestle with today.

Well, what happened after that? Of course, the floodgates were open and the modern welfare state poured through and——

Senator COBURN. Can I get you to go to what do we do about it?

Mr. PILON. Absolutely, and so what we have got today is something like the Labor, HHS, and Education appropriations bill, which I understand is before the Senate today, and again, let me say there is not only no authority for this kind of spending, but there is no authority for even these agencies within the Constitution.

And so the implications of all of this are the loss of legitimacy, legal chaos that flows from this, disrespect for the law, the lack of discipline, and I mean discipline with respect to the Congress itself and discipline with respect to the people, because, of course, if Congress is going to bail the people out every time they get in trouble, you are going to get what you pay for. I give you the example of flood insurance as a perfect example of that. And finally, the economic decline that necessarily follows the expansion of government.

And so what is to be done about this? Well, this isn't going to be changed overnight. We didn't get into this problem overnight. We are not going to end it overnight. Moreover, too many people have come to rely on all of these government programs, so it has to be done slowly, but we have to begin, and the place to begin is with a change in the climate of ideas. Just as the progressives brought about this through a mining of the world of ideas through the early part of the 20th Century, so those of us who want to roll back modern leviathan are going to have to work in the climate of ideas to change it, and one of the best places to start is right here in Congress.

As I said, a decade ago, Congressman Shadegg, Congressman Brownback when he was in the House, Bob Barr, Richard Pombo, and others, there were 100 members altogether in the Constitutional Caucus which sought to revive debate in the House on the meaning and limits imposed by the Constitution. And so this is the first step, to revive constitutional debate by seizing every opportunity, when a bill is introduced, when reauthorization is before the House, to ask, where is the constitutional authority for this?

Second, enact nothing without citing the authority for it in the Constitution and making a clear argument for that.

Third, move toward restoring power back to the States and to the people.

And finally, don't confirm any nominee to the courts who does not understand the Constitution creates a government of delegated, enumerated, and thus limited powers. Thank you, Mr. Chairman.

Senator COBURN. Thank you. Dr. Mitchell.

## TESTIMONY OF DANIEL J. MITCHELL,[1] McKENNA SENIOR FELLOW IN POLITICAL ECONOMY, THE HERITAGE FOUNDATION

Mr. MITCHELL. Thank you, Mr. Chairman. With my testimony already in the record, why don't I just touch on some of the highlights.

Unlike Dr. Pilon, who has the background to discuss the legal issues, I am an economist, so I want to focus more on just the results, the consequences of government spending, and first, let me give a caveat. There are many different policies of government that affect economic performance—trade policy, regulatory policy, monetary policy, and tax policy.

But if we try to isolate government spending and look at the consequences of government spending, the No. 1 thing that one would do is to compare costs and benefits, and the No. 1 thing to do when you are looking at costs is to recognize that you can't spend the same dollar twice. Capital and labor can only be used one time, for one purpose. And so any time government does something, any time it is spending money, any time that money is then being spent in a way that is utilizing capital and labor in our economy, those resources, by definition, are no longer available for other uses. And since we assume that there is some productive capacity in the private sector to utilize resources efficiently, the challenge for policy

[1] The prepared statement of Mr. Mitchell appears in the Appendix on page 80.

makers when trying to estimate the overall economic effect of government spending is to look at what benefits that government spending will generate, or perhaps what costs that government spending will impose.

Economists in the public finance literature talk about public goods. In other words, these are certain goods that have a positive net effect on the economy. We all would recognize or at least appreciate the concept that if you had no government at all and some sort of anarchial system, that you probably wouldn't have very much economic performance. There would be no court system, no rule of law, no police protection, no way for a market economy to function very well in that kind of system. So when you have the public good of police protection, rule of law being put into place, you are actually facilitating private sector economic activity.

It doesn't mean that financing those things is free. It has a cost. But it means that the benefits exceed the cost, and if you look at the back of my testimony, if you have it in front of you, the first chart is something called the Rahn Curve and this is named after a former chief economist for the U.S. Chamber of Commerce who wrote about this back, I think, in the 1980s, he first started discussing this. He makes a point that initial levels of government spending, assuming that they are financing public goods, can have a very pro-growth effect on the economy precisely because they are facilitating the effective operations of a market economy.

But then at some level, when government is finished financing public goods and it starts financing what we traditionally would think of and what Roger described as the modern redistributive welfare state, in that case, you have the cost of raising the revenue, you are displacing private sector economic activity by having government spending money, but you are not getting a commensurate benefit. In other words, you are not financing public goods, you are simply giving money to people for satisfying a certain criteria.

Now, it may be, as has been touched on already, well intentioned, but that doesn't change the fact that there is a real economic consequence. I actually did a review of the academic literature for a paper that was published by The Heritage Foundation on the economic consequences of government spending and it turns out there are several different categories. I won't go through all them here, but suffice it to say that you have two macro economic categories, the displacement effect—government spends a dollar, it is no longer available, and then the financing effect, and that refers to whether you tax a dollar out of the productive sector of the economy or whether you borrow it out of the productive sector of the economy. Those will have specific sectoral effects, the different financing mechanisms. You can even apply that to, if we are a Banana Republic, printing money to finance government spending. That would be a third way, but presumably, we don't do that anymore.

All those different ways of financing government spending impose different negative effects. And then you have the various micro economic effects, and I walk through those in my testimony. It is probably not terribly important to focus on those here.

Instead, let me just take a minute to discuss the actual real world economic effect of these things. I found your chart up there very interesting, comparing the burden of government in the United States compared to the original 15 nations of the European Union. If you look at the actual data for economic performance, and again, keep in mind the caveat there are regulatory reasons, tax reasons, trade reasons that all influence economic performance, and so comparisons between countries are always a little bit tricky. But when you have dramatic numbers, such as the fact that per capita economic output in the United States is 40 percent higher than the average of the European Union 15 nations, that should make us pause and consider, what does that mean?

When you consider that traditional economic theory suggests that if one Nation is poor and another nation is rich, they should begin to converge over time as competitive forces bid away the cost advantages of the lower-income country and raises that country's income. But what has happened is the United States started out richer than Europe and our gap, our lead over Europe has increased in the last 20 years completely contrary to the theory. Why is it that when we are starting out richer than Europe, we are still growing faster than them? Presumably, economic policy plays some role, and presumably, the size of government is one of those economic policies.

If you look at more specific government data, such as unemployment rates, the unemployment rate in the United States is barely half of that of the average in E.U. countries, and some of the most notable welfare States in Europe, like Germany and France, have unemployment rates more than twice the U.S. level.

And perhaps even more shocking is if you look at the duration of unemployment, 48 percent of the unemployed in Europe have been unemployed for more than a year. In the United States, that number is less than 10 percent. Now again, labor law restrictions and rigidities in that market, tax policies, including extraordinarily high payroll tax rates, other factors are involved. We don't want to just focus on government spending.

But in my testimony, from the survey of the academy literature, I walked through some of the key findings, findings not only from academic journals, but findings even from some of the multilateral institutions that we don't normally think of as pro-market—the World Bank, the IMF, the OECD, the European Central Bank—in addition to various academic journals out there, there has been a very clear trend in the academic literature in the last 20 years showing that as government gets bigger, you wind up having a weaker economic performance.

In other words, going back to the theoretical considerations I outlined in the beginning, every time you make government bigger, you not only have those displacement costs, you not only have those financing costs, but then you also have the various and sundry other costs that are outlined in my testimony.

Let me just touch on a few examples of countries that have turned their policies around to conclude my testimony. Oftentimes, when talking about these issues, policy makers will say, but if we dramatically reduce government spending, isn't that going to cause an economic slowdown? Isn't that going to be somehow withdrawing money from the economy? And you walk through, of course, the theory about, no, you are actually freeing up resources for more productive use, but I find it is actually even more effective to talk about real world examples.

New Zealand, many years ago, had government spending at almost 50 percent of GDP. In other words, they were at the level that many European countries are at right now. New Zealand's economy was suffering considerably. Under, actually originally beginning under a Labor Party government, New Zealand dramatically turned around its economic policy, including very significant reductions in government spending. Government spending has now fallen to about 35 percent of GDP, which is pretty close to the U.S. level when you include State and local government in the United States, and what has happened is New Zealand has prospered ever since then. They are now among the top ten competitive economies in the world, according to a whole series of different rankings. Their GDP has increased dramatically and they have clearly turned their economy around.

Ireland is another example. Ireland had government spending of 52 percent of GDP at the peak. Their economy was in the doldrums. Their biggest export was their people. Their unemployment rate peaked at 17 percent. Well, in addition to other policies—again, there are many factors that go into economic performance, but one of the things that Ireland did was dramatically reduce government spending. Indeed, over a period of 1986 to 1988, government spending was reduced by 20 percent. And all told, over the period from the mid–1980s until today, government spending has gone from 52 percent of GDP down to about 33 percent of GDP.

So, in other words, they are one of the European countries that has actually moved much more in our direction, and as a result, the economic consequences for Ireland have been stupendous. Their unemployment rate has fallen from 17 percent to 5 percent and the per capita GDP has expanded so much so that they have gone from being one of the poorest countries in Europe to now being the second richest Nation in the European Union, behind only Luxembourg, which is a special case because it is such a good tax haven for all the other over-taxed people of Europe.

And then, finally, an example from the Eastern Bloc. The former Soviet empire broke up and we now have various nations that are doing a lot of really good things with economic reform. Slovakia is a great example. According to OECD data, in just a period of 7 years, they have brought government spending as a share of GDP down from more than 60 percent of GDP to only about 43 percent of GDP, still very high, but a dramatic reduction in an extraordinarily short period of time.

Now, the old Keynesian theory of government spending being good for the economy would have suggested that would have led to economic turmoil. Instead, Slovakia is one of the new tigers of Eastern Europe and they have more foreign direct investment per capita than any other Nation on earth.

And so again, the actual empirical evidence, the academic evidence, the theoretical evidence all suggests that when government expands beyond the basic financing of public goods—and by the way, it is the public goods that, by and large, are in the enumerated powers section of the Constitution—when government expands beyond that level, there are real economic costs.

Frederick Bastiat, the great French economist, used to talk about or right about the seen versus the unseen, and he was usually talking about why protectionism is bad. We all see the beneficiary of protectionism, but we don't realize, we don't see quite as easily all the people who are losing jobs and losing income because of barriers to trade.

The same analysis applies to government spending. Many people think government spending is good because we see the person getting the check from the government and we think, ahh, that person is going to go out and spend the money in the community and that is going to somehow create jobs. What we don't see is as those resources are displaced from the productive sector of the economy and they are used less efficiently through the political process, there are very real costs, just like there are very real costs to protectionist policies.

Economic growth is all about using resources in the most efficient manner. Having government take those resources, control those resources, and allocate those resources, in most cases, is going to impose more costs than benefits. Thank you very much.

Senator COBURN. Thank you. Let me just ask a question. Did any of these countries—New Zealand, Ireland, or Slovakia—did they develop the political will within, or were they faced with an economic crisis that forced that change?

Mr. MITCHELL. In the case of New Zealand, I think it was an economic crisis from without more than anything else. As a geographically isolated country that obviously had to rely a lot on trade, they were losing foreign investment. They were losing—their own domestic savings was going abroad. And this was actually under the so-called right-wing National Government that these policies really came to a head. That party got voted out of office. The new Labor Party that came in decided that they had no choice but to try to engage in these reforms and they liberalized their economy across the board, not only in terms of spending, but again, I don't want to pretend that spending is the only lever.

In the case of Slovakia, and we have seen this with many other countries to come out of the former Soviet empire, having had their economies decimated by decades of communist rule, they obviously were very ripe for dramatic and sweeping economic reform.

Ireland is a case where, ironically, it seems to have been domestic home grown, where the various parties just came together, and actually, working with business and labor unions, decided if we want to grow and prosper, we better figure out a competitive strategy. As part of being in the European Union, there was a lot of discussion, well, if we can make ourselves the base for multinationals to build their factories to serve the European Union market, that is going to be very successful, and they decided that if they wanted to afford the dramatic tax reductions that they engaged in, they had better also get control of the public spending side of the equation, and so they did the two things in conjunction.

But again, that wasn't really because outside forces were compelling them. There was no IMF or World Bank, like you find with less developed countries, ordering them to make the changes. It was more just that the domestic political forces thought that if we don't make the changes, we are going to continue to suffer migration of our best and brightest young people out of the country. We are going to continue to be the sick man of Europe. We are going to continue to have very low living standards.

Senator COBURN. Do you foresee a potential crisis for this country in terms of the deficit spending, one; international debt, two; and three, international trade deficit, that you could foresee a period of time where there would be economic situations where the international financial community would force those type of changes on this country?

Mr. MITCHELL. Well, I am not one who goes to sleep or wakes up worrying about the deficit. I tend to worry more about just the size of government and how it is financed tends to be a secondary concern. As I mentioned in my testimony, both methods of financing government have their own specific negative sectoral effects on the economy, but having said that, we have a very bleak future in terms of the unfunded liabilities of not only our Social Security system, but Medicare, the new prescription drug entitlement, the combination of all these things. You are looking at unfunded liabilities that are several times the size of the national debt.

Now, again, I am not one that spends a lot of time worrying about the national debt. In present value terms, paying it off today is the same as just rolling it over. That is what interest rates do. They make everything a wash in terms of present value. But when we are looking at projected unfunded liabilities of tens of trillions of dollars, and what that really translates into is the fact that our government spending is going to go up to the level that you find in France and Germany, and whether we decide we are going to finance that government spending by raising taxes or whether we just finance that government spending by issuing debt, assuming people will continue to purchase our debt, the real economic damage is the fact that we are going to have half of our resources in our economy being allocated according to political considerations, and I suspect that is where we are going to do the most damage.

Regarding whether international investors are going to finance our debt, that is a little bit of a tricky question because if you are an international investor purchasing U.S. Government debt—whether you are a foreign life insurance company, a foreign mutual fund, a foreign central bank—we have various sources that are purchasing our government debt, it is obviously not in your interest as a holder of U.S. Government debt to see the value of that debt go down. So I don't think that a foreign central bank or a foreign mutual fund would ever decide that they are going to cause a run on U.S. securities because that would be very much against their interest. They want their investment to grow, to increase, to remain at a high value.

But nonetheless, if we do allow our national debt to grow from, what, around 35 percent of GDP today, if we allow it to go to 50 percent of GDP, 70 percent of GDP, at some point, investors are going to get a little queasy about that. Now, where that point is is hard to say. In a remarkably short period of time, Japan in just the last 15 years has gone from government debt of about 50 percent of GDP to government debt of 120 percent of GDP, but investors are still buying Japanese bonds. The same thing with Italy. Their government debt is well over 100 percent of GDP. It makes ours look like just pennies, and yet people are still buying Italian government debt.

So where that point of crisis occurs, it is hard to say. Where we have seen crises occur in governments tends to be in less developed countries where there is monetization of the debt. That, overnight, will cause the confidence in a country to collapse.

Senator COBURN. Congressman Shadegg, the Enumerated Powers Act is now part of the process, is it not, of the House? How does that work? How did that come about? And do you have any recommendations for us in the Senate?

Mr. SHADEGG. It came about as a result of, I think, the House's decision back even in the heady days of the 104th Congress not to pass a statutory requirement. So instead, it embodied the concept of the Enumerated Powers Act into a House rule. Quite frankly, in my printed testimony, there is a list of bills that were introduced last year where the rule would require citation of the constitutional authority and yet no citation was ever made. I think it is, quite frankly, a feeble attempt to deal with the issue because the rules are known and paid attention to by very few Members of Congress and they are waived routinely by the Rules Committee and tend not to have a very binding or substantial effect on the debate or what goes on.

Quite frankly, I think it is very important in this discussion to recognize that this isn't all green eye shade stuff. My colleague, Mr. Stenholm, talked a lot about the green eye shade consequences and the debate of, well, are tax cuts a bad idea, but spending, we have to hold in control. If we raise taxes and check spending, are we getting somewhere?

I am very pleased to note, as Dan Mitchell points out, that there are economic consequences of an unrestrained government, but there is a more fundamental issue at play here.

It is interesting—again, I point to my colleague, Mr. Stenholm. I, like he, was very pleased the day the House passed the Balanced Budget Amendment saying we should require a balanced budget in this Congress, in this country, and also, like he, was very disappointed when the Senate defeated it. But the reality is, we don't need—we would not need that constitutional amendment if we were simply living up to the Tenth Amendment and the Enumerated Powers Clause and to the restrictions on the powers of Congress.

I think when you begin to see things as radical, for example, as the Nation demanding that the Federal Government take over all disaster response and the President saying, well, maybe we should just cut the locals totally out of that process and maybe what we should do is have a FEMA that simply nationalizes every disaster, I think you begin to see that we have lost all connection, I think, with what the Founding Fathers did.

And I would argue that in so many other places, and I thought Dr. Pilon's comments about how the Supreme Court has created this two-tier interpretation of the Bill of Rights, saying, well, some rights are really important and they point to liberty rights or they point to criminal rights and they say, these just demand or require strict scrutiny, but these other protections in the Constitution, well, they are not so big a deal. We don't have to analyze them so closely.

I think that has gotten us in great trouble because it abandons these fundamental principles. It says, look, sure, we had enumerated powers and they dealt with the growth and size of the government, but that is really not as big a deal as an unlawful search or an unlawful seizure by the police, and so we are going to give closer scrutiny to these. I don't think the Founding Fathers intended that and I don't think they spent their time debating these principles.

Remember, we had previously had an attempt at a National Government. It had failed and we were seeking desperately to strike a balance between the power of the States and the power of the Federal Government. I think a lot of time and energy went into that. I think there are many scholars who say that the authors were inspired, and it is sad to me that we have decided, well, some of the things they were inspired about were important and we will abide by those, but others, such as the Tenth Amendment and Article I, Section 8, well, those aren't so important.

And I think Dan makes the point that once you start to skip—kind of drift a little bit away from those requirements in the Constitution, you can build this massive government and the economic consequences are dramatic.

Senator COBURN. Thank you. Senator Carper.

Senator CARPER. Thanks, Mr. Chairman, and again to our witnesses, thanks for your testimony and for responding to our questions.

I think our Chairman alluded to Davy Crockett. What State was he from, Tennessee?

Senator COBURN. Tennessee.

Senator CARPER. And grew up in Delaware, though, did you know that?

Senator COBURN. He moved West and South. [Laughter.]

Senator CARPER. No, he didn't. Davy Crockett, and Congressman Shadegg referred to him, as well—when I listened to that story, and I have heard it before, what I was struck by was leadership, leadership by example, and what I was struck by was a call for a sharing of sacrifice from across the board from all the members with whom he served, different parties, different parts of the country.

When I look at the situation we find ourselves in today, frankly, I don't see the kind of leadership that I think he epitomized when he stood up and called for what I believe is a sharing of the sacrifice. I think just as his call was answered by his colleagues all those years ago, I believe that a leader today, it is harder for a member of the Legislative Branch to provide that leadership.

Speaking as an old governor, in my State, if governors didn't provide or offer budgets that were balanced, if governors didn't espouse responsible spending programs, if we didn't call for, in my State, rainy day funds, if we didn't call for being conservative on revenue estimates, if we didn't call for those kinds of things, it is not in the nature of a legislative body to step in and fill that legislative vacuum. That is not to take anything away from those of us who have been privileged to serve here, but I would just acknowledge that.

I want to come, first of all, if I could, to Congressman Stenholm. Two of the issues or two of the initiatives that you and I worked on were the Balanced Budget Amendment to the Constitution and what I call a statutory line item veto. And one that you and I worked on in line item veto, I call it a 2-year test drive for line item veto powers, where we give the President enhanced recision powers. Basically, we provided in the first bill that passed when I was in the House with you, provided for a 2-year test drive with the ability for the Congress to override the President's veto or recision with a simple majority, 50 plus one, 50 percent plus one.

The other thing I would note, in our Balanced Budget Amendment, we required—and at the time when we were doing it, I thought all the elements of it were important. I thought it was important for the Congress to be able to override—to unbalance the budget with a three-fifths vote. I thought it was appropriate for us to be able to raise the debt ceiling with a three-fifths vote. But when I look back on our efforts all those years ago, I think maybe the most important provision in our proposal was one whereby the President had to propose a balanced budget.

And I will go back to the idea of executive leadership. My experience in government in my State, and frankly, here and watching State and local governments work, cities and counties work, if you don't have a mayor, if you don't have a county executive, if you don't have a governor, if you don't have a President who is providing leadership by example, it is darn hard to get the legislature or the county council or the city council or the Congress to step up and provide that.

Let me just yield to you, Congressman Stenholm, if I can, and ask you to go back and talk a little bit more about enhanced recision powers, the role of the Executive Branch. How do we make sure that the Executive Branch doesn't misuse those powers in an effort to, as some with whom I serve—Dr. Coburn and I serve with today who are fearful of Congress ceding its powers over appropriations to the President. The fear is that if we give him enhanced recision powers, the President will use those enhanced recision powers to extract from different States, to use those almost to blackmail Senators and Representatives to support positions that we otherwise would not. Would you just comment on those, please?

Mr. STENHOLM. Yes. One of the thought processes and legislative processes that I went through over the years leading up to that, first off, there was tremendous support for the line item veto in certain groups, the more conservative groups saying, we ought to give the President line item veto.

I opposed that and I always asked anyone this simple question. Does it matter to you, and I usually used the word "President Kennedy" or "President Reagan," does it matter who it is you are going to give the line item veto? If they said, no, it doesn't matter, fine, that is an honest position. But if you hesitate for just a moment, depending on whether you are looking at a liberal President or a conservative President—the eye is in the beholder—then I have got concern with that.

Therefore, we came then ultimately to saying that it doesn't matter to me—it matters to me a whole lot. I don't want to give any President one-third plus one minority override of the Congress of the United States. I did not want to do that. It didn't matter who the President was. But since we get into this debate about spending, and we are into it again, and I think it is fascinating that at no time in the last 5 years has there been any recision of any spending. We are talking about leadership and accountability. Say that respectfully, now.

I am a great respecter of the office of the President of the United States, but if we were having this discussion today and we Democrats were in the majority, I suspect there would be a different tone of the concern of the deficits today, with all due respect to Heritage and Cato, who I have found to be tremendously credible. I will say over the years, my 26 years, both of these organizations have performed a tremendous service for those of us privileged to serve in the Congress with the battle of ideas. I don't agree with them 100 percent of the time, but I think I can say that I have agreed a majority of the time, 50 percent plus one.

But having said that, I came down to basically this. I don't mind giving any President line item veto modified, by that saying that if he picks out something that Charlie Stenholm put into the budget, into the appropriations, somewhere there, and the President says, no, it should not be there, all I want is a chance to have 50 percent of my colleagues to agree with me. If they agree with the President, it ought to go.

I think that is something that gives transparency to accountability. That was the process we went through, and I think it is still a very good process because it does bring accountability and transparency to many of these issues and it also would cause those, if you are going to ask for something to be in the budget, you have to be prepared to defend it in the context of your colleagues, 50 percent plus one.

Senator CARPER. Thanks very much.

If I could, Dr. Mitchell, I just may direct a question to you. I probably should know these numbers better than I do, but my understanding is that revenues to the Federal Government as a percentage of GDP go up and down, sometimes as high as maybe the low 20 percent, sometimes as low as 17 percent, at least in my lifetime. I am 58 years old. And probably during World War II, that percentage was well above 20, 22, 25 percent during that period of time.

Today, we are spending, I am told, about 17.5 percent—revenues constitute, rather, about 17.5 percent of our GDP. I think compared to the last 10, 20, maybe 30 years, that is fairly low. If you look at the difference between revenue as a percentage of GDP at 17.5 percent, spending as a percentage of GDP is about 20.5 percent. Those 3 percent, I think, pretty much account for a $315, $320 billion deficit. Some would argue that if we just raised revenues by those 3 percent, we would be able to balance the budget.

I don't buy any of that argument. I think there is plenty that we can do. Dr. Coburn and I are interested in—not just interested, but we are working hard to clamp down on improper payments. Those are probably worth about $50 billion a year. We are about to go to work on making sure that the revenues that are owed, that we know who owes the revenues that are not being collected and that is at least $100 billion a year, maybe twice that, that we go after that. Congressman Stenholm has talked about trying to make sure that we are using the right COLA that we use to adjust payments. I know I suspect all of us are supporters of BRAC as an effort to try to cut some spending out there. I have been working on flood insurance for 15 years, trying to make sure we don't reward people for building in harm's way. There is a whole lot of stuff we can do, means testing both parts of Medicare and maybe Medicaid, trying to make sure that folks don't dump their assets in order to be eligible for Medicaid. There is a whole lot that we can do other than just raising revenues to close that deficit. So I wouldn't suggest that we reduce the entire deficit, but if we could think about it, if we could actually make sure that $50 billion worth of improper payments didn't get paid every year, if we could even collect half of the $200 billion that we think is out there to be collected but not being collected, and if we could do some of these other things that I mentioned, the difference between revenue as a percentage of GDP and spending as a percentage of GDP wouldn't be 3 percent. It would be a whole lot less than that.

So that is a long way of asking this question. Do you see any rationale for raising revenue as a percentage of GDP, or how would you practically go about reducing that difference, that 3 percentage points? How would you propose that we do it other than some of the things that I have mentioned?

Mr. MITCHELL. If you look at the last 50 years, basically from the end of World War II until today, Federal tax revenues have averaged 18.1 percent of GDP. We are a little bit below that now, so if you look at the CBO long-range forecast, even with the President Bush tax cuts being made permanent, we are supposed to sort of slowly creep up to about that level. Now, that still begs the issue of, OK, well, spending is at 20.5 percent of GDP and even if we are at our long-term average of revenues, what needs to be done?

I, of course, would prefer, looking at the economic data, the economic literature, that we reduce the size of government. Now, that doesn't take, I think, too much heavy lifting. If revenues are going to grow just normally, 7 percent a year in nominal terms, which means about 4 percent, say, in real terms, if we can somehow just limit government growth to twice the rate of inflation, we would pretty quickly get to a balanced budget for those that think a balanced budget is nirvana.

Again, as I stated before, I am not sure it is nirvana. Norway, in large part thanks to oil revenues, has a budget surplus, but government spending is at 50 percent of GDP and they are suffering a lot of economic problems. They just happen to have the revenue to finance that government, but I don't think that is—we wouldn't want to trade places with Norway. Maybe we would like their oil, but we certainly wouldn't want to trade places with their fiscal policy.

In terms of whether revenue should be higher than 18 percent of GDP, I am tempted to say no, but let me cite an example of how I would say yes. Hong Kong has a 16.5 percent flat tax. The tax revenues in Hong Kong are a little bit more than 20 percent of GDP.

I would be perfectly happy to trade tax systems with Hong Kong. I suspect the lower incentives to evade and avoid the tax system, the faster economic growth—Hong Kong has been the fastest-growing economy in the world ever since the end of World War II—for a whole host of reasons, we could wind up collecting more revenue, but it wouldn't be as a result of imposing additional burdens on the American people. It would be the result of having a tax system that just facilitates and makes it easier for an economy to grow and for people to pay their taxes without having nearly the incentive to utilize lawyers, lobbyists, accountants, financial planners, and people like that to minimize their tax bills, either legally or illegally.

So in that special circumstance of utilizing better tax policy to get additional revenue, you could get a "yes" out of me, but as a general rule, no, I don't think the problem we have is a problem of too little revenue coming from the American people.

Senator CARPER. Thank you very much.

Senator COBURN. Thank you.

I tend to recall a graph I saw on economic growth in the United States, and every time that tax revenue got above 19 percent of GDP, economic growth declined. Every time it was below 19 percent, economic growth grew, and that is on a trend line from, I believe, 1951 forward. So 19 percent somehow in our economy seems to be the cutoff at which, when tax revenues rise to that level, we see an impediment to economic growth.

I wanted to clear up some things, because I think one of the problems in Washington that has caused some of our problems is we don't talk real numbers. We have had people talk today about the deficit. You all have mentioned the deficit. But, you know, the real number that impacts our economy is not the deficit. The real number that impacts our economy is how much do we add to the debt every year, and what we publish as the deficit versus what we add to the debt are two totally different numbers.

One of the things that I would just like to add, we really ought to be talking about the real numbers because the deficit doesn't include any off-line emergency spending, which goes straight to debt. We never put that in the number. So when we are comparing—for example, this year already, we have passed almost $200 billion of emergency spending, of which a large portion of that, or $100 billion, if you look at that into the real deficit this year, that is close to $500 billion in terms of increased debt that our kids pay. So I think part of our problem is the numbers we use.

An interesting thing that we have found also is our budget scoring rules cause us to do the wrong thing economically. For example, we no longer lease-purchase any buildings in the Federal Government. The reason we don't lease-purchase any buildings in the Federal Government is because if you lease-purchase it, it is scored as a cost to the year that you signed the lease-purchase rather than amortized over the lease-purchase. So we lose two ways. One is, first of all, we don't have any ownership. Two, we lose in the appreciation of the asset. That is about $3 billion a year we are losing right now because we lease rather than lease-purchase, and it is sort of our oversight.

The other thing that I wanted to bring out is there is a real difference, and a philosophical difference, as Crockett called for shared sacrifice. He didn't call for the government to do it through forced sacrifice of other people. He called for shared sacrifice of individuals. There is somewhat of a philosophical difference between the two sides of the aisle on where that sacrifice should come, and the thing that I have talked about with Katrina is that charity cannot be made without real sacrifice.

So I am tremendously thrilled with the testimony we have had today and I want to thank each of you for being here, and especially Congressman Shadegg. This was a real sacrifice on his part on things he needed to do in Arizona and he gave those up to come and testify and I want to tell you, John, I appreciate it.

Congressman Stenholm, I want to offer a formal request that you come and visit with me. I believe in pay-as-you-go. I believe in doing the right things and I believe we ought to institute everything we can to put fiscal discipline back within us.

But I would also say, we don't need any of that if we will just follow the Constitution, because if we follow the Constitution, we won't have to have an expedited recision. There won't need to be one because we won't be putting it up there if it is not a constitutionally valid piece of legislation in the first place. We saw what happened in the Senate this last week is that when you—this whole theory of earmarks. Earmarks in the long run hurt us all. They don't help us. They hurt us all, because the sum of the whole is much less of what the States get versus the damage that is caused by earmarks.

So we have a lot of work to do before us. I thank you for your testimony. I look forward to hearing and working with each of you in the future, and the hearing is adjourned.

[Whereupon, at 4:16 p.m., the Subcommittee was adjourned.]

# APPENDIX

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## GETTING SERIOUS ABOUT DEFICITS?

### Calls to Offset Hurricane Spending Miss the Point; Balanced Set of First Steps Toward Fiscal Discipline Needed

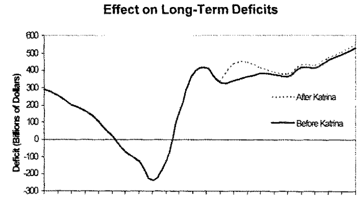
by Robert Greenstein

Discussions have started in recent days about offsetting some or all of the expenditures that the federal government will need to make for relief and recovery from the recent hurricanes. From the standpoint of safeguarding the nation's fiscal health, these discussions often seem inconsistent and confused.

Many policymakers speak of the need to offset hurricane-related expenditures as though those expenditures pose a serious threat to the nation's fiscal well-being. Yet most economists and fiscal policy analysts agree that those costs do not by themselves represent such a threat, as long as the costs remain temporary and end once the relief and reconstruction job is done.

**FIGURE 1**

**Hurricane Katrina Will Have Little Effect on Long-Term Deficits**




Projected deficits come from the CBO August Baseline, adjusted for extension of the Bush tax cuts and a phase down of spending in Iraq

The real threat to the nation's fiscal — and ultimately, its economic — health is posed by the large mid-term and long-term deficits that loom as far as the eye can see. One-time costs for hurricane relief and reconstruction will worsen this problem only to the extent that they increase the interest costs the government will have to pay in future years as a result of having borrowed money to finance the hurricane-related activities. If we spend $200 billion for hurricane costs (and the likely amount now looks smaller than that) and borrow the entire amount, the projected deficit ten years from now will be about 3 percent higher than it otherwise would be, as a result of these added interest costs. This is not a large amount.

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**Claims that Hurricane-related Costs Will Drive Federal Spending to Unusually High Levels Are Incorrect**

Policymakers who call for offsetting the costs of hurricane-related expenditures, but not of hurricane-related tax cuts or other, more long-lasting tax cuts, often argue that the expenditures being made in response to the hurricane are contributing to a dangerous explosion of federal spending. Such a claim is misguided.

- Even if we spend $200 billion for hurricane-related costs over the next few years (a figure that now seems too high), federal spending will average 20.1 percent of the Gross Domestic Product from 2006 through 2010. (This estimate includes the costs of operations in Iraq and Afghanistan and implementation of the new Medicare prescription drug benefit.)

- That level will be *lower* than the average level of federal spending, as a share of GDP, over the past 30 years.

The deviation from recent historical patterns continues to be on the revenue side of the budget, rather than on the expenditure side. Revenues remain unusually low as a share of the economy due to the large tax cuts of recent years. (Eventually, expenditures will surpass historical averages as the population ages and health care costs continue to rise, but that is not the case today.)

Indeed, the cost over the next five years of the tax cuts enacted in 2001 and 2003 will be $1.77 trillion (assuming that the provisions of those tax cuts that are scheduled to expire before 2010 are extended). This is *more than seven times* the anticipated costs related to the hurricanes.

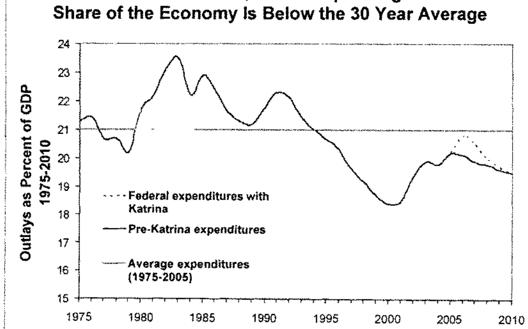
This is the reason that the budget enforcement rules of the 1990s, which contributed to the elimination of deficits during that decade, required entitlement increases and tax cuts to be offset but provided an exemption for one-time emergency spending. The one-time expenditures that the federal government incurred in response to those disasters that occurred during the 1990s did not prevent the achievement of a balanced budget in that decade.

Adding further to the confusion surrounding the current debate is that many policymakers who speak of the need to offset hurricane-related *expenditures* do not appear to be calling for similar offsets for the cost of hurricane-related *tax cuts*. Both the expenditures and tax cuts will add to short-term deficits.

Of greatest concern is the fact that some policymakers seem to be calling for offsetting the costs of *temporary* hurricane-related expenditures while planning to proceed with measures that will increase deficits *on an ongoing basis*, such as measures to extend tax cuts with an eye to later making them permanent, and doing so without offsetting the costs. Seeking to offset one-

**FIGURE 2**

**Even with Katrina, Federal Spending as a Share of the Economy Is Below the 30 Year Average**



time emergency expenditures that will have little bearing on future deficits, but *not* to offset other policy actions that will make mid-term and long-term deficits even larger, stands sound fiscal policy on its head. From the standpoint of restoring fiscal discipline, such an approach is upside down.

Furthermore, some who are calling for budget cuts to offset the hurricane-related spending reportedly favor focusing those cuts heavily on basic assistance programs for the poor, such as Medicaid, food stamps, and welfare reform funding, even as tax cuts primarily benefiting high-income households are extended and further enlarged.[1] Asking Americans at the bottom of the income scale to bear the heaviest burden in offsetting the hurricane-related costs seems inconsistent with the President's declaration, in his nationwide address on September 15, that "we have a duty to confront this poverty with bold action."

One example of the confusion that surrounds the current debate is the call by the Republican Study Committee, a group of the House of Representatives' most conservative members, for a one-year delay in implementing the Medicare prescription drug benefit as a way to offset some of the hurricane-related costs. Under the RSC proposal, the prescription drug legislation would take effect in its current form, without any economies being achieved in it, but with the start date pushed back 12 months to January 1, 2007. Such an action would have *virtually no discernible effect* on mid-term and long-term deficits. A much sounder approach involving Medicare would be to allow the drug benefit to take effect as scheduled on January 1, 2006, but to make changes in that legislation and other Medicare rules related to the Medicare payment system to reduce Medicare costs *on an ongoing basis.* In June, the Medicare Payment Advisory Commission, Congress' official expert advisory board on Medicare payments, warned that billions of dollars of excessive and unwarranted payments will be made to managed care companies under the prescription drug legislation and other Medicare rules, and that Congress should act to fix this problem. MedPAC recommended changes that would save $20 billion to $30 billion over five years and continue producing savings after that. Action to correct these overpayments would make much more sense than a one-year delay in the drug benefit.

The debate about offsetting the costs of hurricane relief and reconstruction thus has the potential to be a distraction from the real fiscal problems that the nation faces. Yet this debate also could present an opportunity for policymakers finally to start addressing the nation's deep fiscal problems. Accordingly, this analysis discusses initial steps that policymakers can, and should, take to begin dealing with the daunting fiscal challenges that the nation faced even before the hurricanes — and that it continues to face now.

### What Should be Done?

The nation needs major action by policymakers to put all parts of the budget — including revenues — on the table, to invoke a spirit of "shared sacrifice" and a willingness to target "weak claims" rather than "weak clients" (to use the felicitous phrase of David Stockman, President Reagan's first budget director), and to start making tough choices. Sadly, action of this nature does not seem likely at the present time.

[1] Several news accounts have reported that House Republican leaders and leaders of the Republican Study Committee plan to focus cuts to offset the hurricane-related costs on Medicaid, food stamps, welfare reform, as well as across-the-board reductions in non-defense discretionary programs outside homeland security. See Ben Pershing, "GOP Still Seeking Spending Cuts," *Roll Call*, September 28, 2005; and John Stanton, "Frist, GOP Leaders Move to Regain Footing in Debate Over Katrina Relief Spending," *CongressDailyAM*, September 28, 2005.

But policymakers can at least do two things now. First, they can take action to stop digging the long-term deficit hole deeper. Second, they can consider a balanced package of initial steps to start reducing the large long-term deficits that lie ahead. The remainder of this paper examines what policymakers could do in each of these areas.

## Stop Digging the Hole Deeper

Three steps should be taken here. Policymakers should reinstitute the "Pay-As-You-Go rules" that worked effectively in the 1990s. They should drop plans to use the fast-track "reconciliation" process in coming months to *increase* deficits. And they should forgo implementing scheduled tax cuts that have not yet taken effect unless the cost of those tax cuts is fully offset.

### 1. Reinstating the "Pay-As-You-Go" rules

In 1990, the first President Bush and Congressional leaders of both parties designed rules to require entitlement expansions and tax cuts (including extensions of supposedly temporary tax cuts) to be "paid for" through offsetting entitlement reductions or tax increases. (The rule contained an exception for expenditures or tax relief to meet emergency needs, such as relief and recovery from hurricanes, earthquakes, and other disasters.) This rule worked effectively through most of the 1990s, until budget surpluses emerged. It kept entitlement increases and tax cuts from enlarging the deficit, and it contributed to the remarkable improvement in the fiscal outlook that occurred in that decade. Virtually all of Washington's principal "budget watchdog" organizations — the Concord Coalition, the Committee for Economic Development, the Committee for a Responsible Federal Budget, and the Center on Budget and Policy Priorities — have called for a return of these rules. So, on repeated occasions, has Federal Reserve Board Chairman Alan Greenspan. Such a step is long overdue.[2]

### 2. Dropping this year's reconciliation legislation

The fast-track budget "reconciliation" procedures were originally designed to facilitate the passage of deficit-*reduction* legislation, by preventing such legislation from being subject to a filibuster in the Senate. In recent years, the original intent of reconciliation has been stood on its head, with the reconciliation procedures used to push through deficit-*increasing* legislation.[3]

Unfortunately, this year's reconciliation directives continue that trend. The Congressional budget resolution adopted this spring calls for using the reconciliation process to pass legislation that would increase deficits by more than $35 billion over five years. The intended reconciliation legislation would include $35 billion in entitlement reductions and $70 billion in tax cuts, for a net increase in the deficit of $35 billion. (The actual increase in the deficit would be slightly larger because of the added interest payments on the debt that would have to be made.)

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[2] A reinstated Pay-As-You-Go rule should retain the emergency exception. Such an exception allows for an immediate response to devastating events like Hurricanes Katrina and Rita. As demonstrated by the progress during the 1990s from budget deficits to budget surpluses, such an exception does not significantly diminish the effectiveness of the Pay-As-You-Go rule.

[3] Both the 2001 and 2003 tax cuts were passed through use of the reconciliation procedures.

Apparently to mask the fact that the planned entitlement reductions — many of which would come in programs for the poor — would be used *not* to reduce the deficit but to defray a portion of the cost of the tax cuts, Congressional leaders this year split reconciliation into two bills: a bill intended to cut programs such as Medicaid, food stamps, and student loans, and a separate tax-cut bill. The two reconciliation bills are slated to move one week apart from each other. This cosmetic step, however, does not alter the bottom line — this year's reconciliation legislation would increase deficits.

Adding to the disturbing nature of this use of the reconciliation process is the fact that it would likely increase hardship among poor Americans — potentially making people below the poverty line pay more for essential health care services and medications, and cutting food stamp benefits that already average only $1 per person per meal — in order to cover a portion of the cost of tax cuts that would go disproportionately to the most affluent people in the country. A centerpiece of the tax-cut reconciliation bill is expected to be an extension of the capital gains and dividend tax cuts that were enacted in 2003 and are slated to expire at the end of 2008. The Urban Institute-Brookings Institution Tax Policy Center reports that 53 percent of the benefits from these two tax cuts are going to the 0.2 percent of Americans who make over $1 million per year.

Instead of moving reconciliation legislation that would increase deficits while heightening hardship among those at the bottom of the income scale, Congress should identify those tax cuts slated to expire at the end of 2005 that need to be extended — such as relief from the Alternative Minimum Tax — and extend them *outside* of the reconciliation process, through legislation in which their costs are offset, in accordance with the Pay-As-You-Go principle. A number of revenue options for offsetting the costs of these tax-cut extensions are available.

For example, in January 2005, the Joint Congressional Committee on Taxation — Congress' official source of analysis, cost estimates, and advice on tax policy matters — issued a major report detailing options to achieve $190 billion in revenues over five years and $400 billion over ten years from closing unwarranted or unproductive tax breaks and improving tax compliance. Not all of the Joint Committee's proposals would garner widespread support. But some are common-sense ways of closing especially dubious tax loopholes or curbing tax avoidance.[4] Revenues from a modest fraction of the Joint Committee's proposals could offset the costs of extending tax cuts that are expiring and need to be extended now.

**3. Shelving upper-income tax cuts that are not yet in effect**

Recent tax cuts for upper-income Americans have been generous. The Urban Institute-Brookings Tax Policy Center reports that households with incomes of over $1 million are now receiving tax cuts from the 2001 and 2003 tax-cut legislation that average $103,000 a year. Nevertheless, on January 1, 2006, two costly *new* tax cuts that will exclusively benefit high-income households — and that were not requested by President Bush — will start taking effect for the first time. The nation cannot afford additional upper-income tax cuts. Accordingly, these tax cuts should be cancelled.

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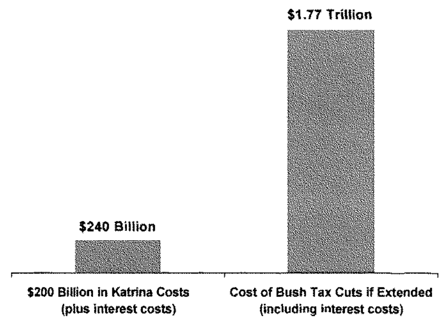
[4] For example, the Joint Committee recommended that some taxes be withheld when the federal government and state and local governments pay for goods and services. Such withholding would raise revenues by promoting improved tax compliance. Another Joint Committee proposal would require courts to apply tests to certain uncommon transactions to ensure these transactions are being undertaken for real business purposes rather than for tax-avoidance reasons.

(Alternatively, if policymakers are determined to institute them, their costs should be offset through reductions in other tax cuts for those at the top of the income scale.)

FIGURE 3

Cost of Katrina Expenditures and Administration Tax Cuts, 2005-2010
(includes cost of interest payments on the debt)




The two new tax cuts in question were enacted in 2001, when Congress added them to the tax package that President Bush submitted. Congress used a budget gimmick to fit the costs of these two measures into the overall amount available to it for tax cuts that year — it pushed off the start of these two tax cuts until 2006 and then phased the two tax cuts in gradually so they would not take full effect until 2010. That way, little of their cost appeared in the ten-year budget window that was being used to measure the cost of the 2001 tax-cut legislation.

One of the two new tax cuts in question repeals a provision of the tax code under which the personal exemption is phased out for people at high income levels. (This is sometimes referred to as the "PEP," or personal exemption phase-out, provision.) The other new tax cut repeals a provision of the tax code under which limits are placed on the total amount of itemized deductions that taxpayers with high incomes may claim. (This is referred to as the "Pease" provision, after the Congressman who originally designed it.) Both of the tax-code provisions that the new tax cuts would repeal were signed into law by President Bush's father as part of the landmark, bipartisan deficit-reduction law of 1990.

The scheduled implementation of these two new tax cuts on January 1 will benefit only households at high income levels. The Urban Institute-Brookings Tax Policy Center reports that when these two tax cuts are fully in effect, 54 percent of their tax-cut benefits will go to households with income of over $1 million a year, with those households getting an average annual tax cut of $19,200 from these two measures. The Tax Policy Center also found that nearly all (97 percent) of the benefits from these tax cuts will go to the 3.7 percent of households that have incomes of more than $200,000. The remaining three percent of the tax-cut benefits will go to households with incomes between $100,000 and $200,000, but the tax cuts will do little for most of those people; for households in the $100,000-$200,000 range, the average tax cut will be just $25.[5]

But while only a small slice of very affluent Americans will benefit substantially from these new tax cuts, the cost will be substantial. Assuming the two tax cuts are extended beyond 2010, the cost of these tax cuts will be *$146 billion* over the first ten years they are in full effect (2010 through

[5] A modest number of households in the $75,000 to $100,000 range also will get tiny tax cuts from these two tax-cut measures. The average annual tax cut for households in this income range will be $1.

2019). When the added interest payments on the debt are taken into account, the total cost of the new tax cuts rises to nearly $200 billion over that ten-year period.

Thus, by 2020, the cost of the two new tax cuts, if extended, will roughly equal the total costs of relief and reconstruction from the recent hurricanes. Over the longer term, the cost of these new tax cuts will dwarf the costs resulting from the hurricanes. Shelving tax cuts such as these that are not yet in effect and that the nation cannot afford should be a basic component of efforts to stop digging the deficit hole deeper.

## Initial Steps to Start Filling in the Hole

As noted earlier, major bi-partisan efforts ultimately will be needed to make large-scale progress on the long-term fiscal problems the nation faces. Legislation will be needed to address the high and relentlessly rising costs of the U.S. health care system, to restore Social Security solvency, and to raise significantly more revenue. Unfortunately, such measures do not seem politically possible now. But policymakers should at least consider a balanced package of initial steps. Such a package would include both spending restraint and revenue enhancements. A package of initial, deficit-reduction measures could include the following.

### 1. Instituting MedPAC's recommendations to rein in excessive payments to certain Medicare managed care plans

The Medicare Payment Advisory Commission (MedPAC), the official, independent advisory body to Congress on Medicare payment policy, issued a major report in June 2005 that calls for changes in how the Medicare program sets payment levels for managed care plans. MedPAC identified a large volume of excessive and wasteful payments that are being, or will be, made to such companies as a result of inefficiencies in the Medicare payment structure. (In some cases, the excessive payments result from mandates that Congress has imposed on the Medicare program at the companies' behest.) MedPAC found that the excessive payments not only raise program costs but also tilt the "playing field" in favor of the companies receiving the excess payments, and accord those companies an unfair competitive advantage over traditional fee-for-service Medicare in seeking to attract patients. The MedPAC recommendations are based on extensive analysis of the amounts that Medicare pays different types of managed care plans and traditional fee-for-service providers to deliver the same health care services.

Congressional Budget Office estimates show that the MedPAC recommendations would save $20 billion to $30 billion over five years. The MedPAC recommendations include:

- Eliminating extra payments to certain new regional Preferred Provider Organizations, which will be *on top* of these PPOs' regular Medicare fees and will place the total fees these PPOs receive above the fees paid to Medicare HMOs and the amounts spent to provide comparable services through traditional fee-for-service Medicare;

- Setting the base payment levels for all Medicare managed care plans (including both the new PPOs and Medicare HMOs) at the same level that it costs to treat beneficiaries with comparable health conditions through traditional Medicaid fee-for-service arrangements, rather than paying the managed care companies *more* than it would cost to treat the same patients through traditional Medicare; and

- Ending the practice under which the federal government essentially pays *twice* for some of the costs that teaching hospitals incur. Medicare pays twice for some of the costs that teaching hospitals incur in treating Medicare beneficiaries who are enrolled in managed-care plans, because Medicare makes an upward adjustment to cover these costs *both* in the payments that it makes directly to the hospitals *and* in the payments that it makes to the managed care plans that enroll these beneficiaries.)

**2. Reforming agricultural subsidies**

Mandatory spending on farm price support and income support programs is expected to total about $21 billion this year. Most independent policy analysts across the political spectrum agree that much of this spending is inefficient or unnecessary. A great deal of it goes to very large agricultural entities, not to small family farmers. Producers of some crops receive generous subsidies while producers of other crops get none.

Some of these subsidies (and some similar subsidies in other countries) also distort international markets and are a target of World Trade Organization efforts to liberalize would agricultural markets. Of particular concern, some of these subsidies apparently contribute to the depth and breadth of severe poverty and hunger in some of the world's most impoverished countries by tilting markets away from poor farmers in those areas.

Various proposals have been made to reform the agricultural subsidies. One set of reforms is included in the budget that President Bush submitted in February. The Congressional Budget Office estimates that the President's proposals to reform agricultural subsidies would save $7.5 billion over five years and $17.1 billion over ten years.

**3. Paring back the earmarks in the highway bill**

The recent highway legislation contains more than 6,300 earmarked projects at a total cost of over $22 billion, according to the Congressional Research Service. While some of these projects may be meritorious, others are not. CRS notes that of the congressional earmarks, 5,145 were designated as "high priority projects," which is almost three times as many as the 1,849 similarly labeled projects in the previous highway bill.

A project that has gotten considerable play in the national press consists of two earmarks totaling $175 million to construct a bridge from Ketchikan, Alaska (pop. 13,000) to Gravina Island, Alaska (pop. 50), where the local airport is located. Tens of millions more would go for other, related projects in and around Ketchikan. According to the organization Taxpayers for Common Sense, the bridge would be taller than the Brooklyn Bridge and nearly as long as the Golden Gate Bridge and would replace the need for residents to reach the airport by taking a $6 ferry ride lasting seven minutes.

Highways are not the only source of wasteful or low-priority projects. According to a joint report by the National Wildlife Federation and Taxpayers for Common Sense, the budget of the Corps of Engineers includes numerous projects that either have little merit or would actually be harmful. The report lists projects such as the Grand Prairie irrigation project in eastern Arkansas at $319 million and the Big Sunflower River Dredging Project and Yazoo Backwater Pump at $243 million. According to the report, these projects and others like them would do significant environmental harm, are not designed to protect populations or property from floods, and would have only minor and local economic benefits that do not justify the costs.

### 4. Paring back special-interest tax breaks and expenditures in the recent energy and corporate tax bills

Over the past year, Congress has enacted two tax-cut packages laden with ill-advised targeted tax breaks — the corporate tax package in October 2004 and the energy bill in July 2005. Despite supporting the corporate measure, the Bush Administration complained bitterly about "a myriad of special interest tax provisions that benefit few taxpayers and increase the complexity of the tax code" that were inserted in the House and Senate bills.[6] Many of these provisions were retained in the final measure, including special tax breaks for ceiling fan importers, horse and dog racing, NASCAR, restaurants, and railroads, to name a few. Even the measure's centerpiece tax cut for domestic manufacturers was so distorted by the end of the process that it, too, deserves "bad marks," according to Congressional Research Service economist and tax expert Jane Gravelle, because it distorts investment decisions and imposes significant administrative and compliance costs.[7] In total, the measure included $130 billion of tax cuts between 2005 and 2014. Canceling just a fraction of these measures would yield significant savings.

The energy bill also included a number of special-interest tax breaks. For instance, the measure gave write-offs for electricity transmission equipment, natural gas pipelines, and oil refiner equipment, and provided tax credits for nuclear power production and clean-coal technology. (Taxpayers for Common Sense has compiled a list of dubious tax breaks and spending contained in the energy bill.[8])

The oil and gas producers who will benefit handsomely from the measure already pay federal taxes at a very low rate. Between 2001 and 2003, the federal taxes of the petroleum and pipeline companies in the Fortune 500 list averaged only 13.3 percent of their earnings, well below both the 35 percent corporate tax rate and the average effective tax rate for other industries.[9]

The special interest provisions in these bills should be reexamined and the bills' costs pared back.

### 5. Ending other unproductive tax breaks, curbing tax shelters, and attacking tax avoidance

As noted earlier in this paper, Congress' Joint Committee on Taxation issued an important report in January 2005 setting forth a series of specific options to eliminate questionable or unwarranted tax breaks and to help curb the extensive tax avoidance that now occurs. Taken as a whole, these

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[6] Letter from Treasury Secretary John Snow to Rep. William Thomas, October 4, 2004.

[7] Jane Gravelle, "The 2004 Corporate Tax Revisions as a Spaghetti Western: Good, Bad, and Ugly," April 2005, presented at the National Tax Association Spring Symposium, May 19-20, 2005.

[8] Taxpayers for Common Sense, "Top Ten Worst Provisions in the $85 Billion Conference Energy Bill," July 27, 2005.

[9] Citizens for Tax Justice, "Conference Committee Energy Bill Rewards Corporate Tax Avoiders, Creates Conflicting Incentives," July 28, 2005.

options would save about $190 billion over five years and $400 billion over ten years. Some of the Joint Committee's options would require taking on "sacred cows" and do not appear politically feasible. But numerous other options warrant serious consideration. Substantial savings could be at stake.

### 6. Reducing spending and raising revenues by using a more accurate measure of inflation

A number of federal entitlement programs, including Social Security, provide benefits that are adjusted each year to keep pace with inflation, as reflected in the Consumer Price Index. A number of features of the tax code also are adjusted annually for inflation, in accordance with changes in the CPI.

Research indicates that the CPI slightly overstates inflation. This is a judgment that most experts — including analysts at the Bureau of Labor Statistics, which maintains the CPI — share.

Accordingly, the Bureau of Labor Statistics has developed an alternative CPI, sometimes known as the "superlative CPI" or the "chained CPI," which takes into account the tendency for consumers to buy more products whose prices have increased slowly and fewer products whose prices have increased rapidly. (For example, people who ordinarily purchase beef twice a week may switch to pork or chicken if the price of beef rises too high and the price of chicken or pork remains low.) The BLS began to issue inflation estimates using both the traditional CPI and this new "superlative CPI" in the summer of 2002. The superlative CPI is expected to rise, on average, about two-tenths of one percentage point less per year than the traditional CPI.[10]

It is a basic principle of federal policy that Social Security and other benefits should keep pace with inflation so that program beneficiaries do not lose ground as the years go by. Another basic principle is that the tax code should be adjusted for inflation so that taxpayers are not pushed into higher tax brackets or do not otherwise have their tax bills raised solely because of inflation. These principles surely should be maintained. But there is no need to adjust benefits or tax-code features by more than inflation.

Congress could address this matter by requiring that the programs and the parts of the tax code that are adjusted for inflation in accordance with the CPI by adjusted from now on in accordance with the superlative CPI. Such a change is best viewed *not* as a benefit cut or a tax increase, but as more of a technical change to achieve Congress' stated goal of keeping pace with inflation in as accurate a way as possible.

In any year, the effects would be very small. Cost-of-living adjustments would on average be about two-tenths of a percentage point below what they would be if the old CPI were used. The long-term effects on the budget would be larger, however, because the effects would compound over time. In the 2004 Brookings Institution volume *Restoring Fiscal Security* (which also calls for this change), Brookings analysts estimated that if this change had taken effect in 2005, it would save about $35 billion a year by 2014, with those savings about equally divided between the program and revenue sides of the budget.[11]

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[10] The Social Security actuaries estimate the average annual difference to be 0.22 percent.

[11] Alice M. Rivlin and Isabel Sawhill, eds., *Restoring Fiscal Security*, the Brookings Institution, 2004, page 42.

The savings would continue to grow in years after 2014. This proposal thus has the virtue of phasing in slowly and producing savings that grow over time as the fiscal picture is darkening. In other words, the savings would mount as the need for savings increased.

It should be noted that over the past decade, the Bureau of Labor Statistics has made a number of other changes directly in the CPI itself that have significantly reduced the degree to which the CPI overstates inflation. These changes, which in combination are more than twice as large as the change proposed here, have been non-controversial. They have been incorporated directly into the official CPI and have affected the annual adjustments in Social Security, other programs, and the tax code *without* arousing opposition or protest. For technical reasons, the Bureau of Labor Statistics cannot incorporate the modest improvement reflected in the superlative CPI directly into the official CPI. That is why the BLS developed the superlative CPI alongside the traditional CPI.

This proposal also has one other benefit — by causing Social Security expenditures to be modestly lower than they otherwise would be, it would contribute to restoring long-term Social Security solvency. According to the Social Security actuaries, this proposal would close nearly one-fifth of Social Security's long-term (i.e., 75-year) financing shortfall. (Under Congressional Budget Office estimates, the proposal would close about one-fourth of the shortfall.) The eminent Social Security expert and sage Robert Ball has endorsed this change as one of the steps that should be taken to restore Social Security solvency.[12]

## Conclusion

Despite the flurry of recent statements about offsetting costs related to the hurricanes, there is little sign that policymakers are getting serious about mid-term and long-term deficits. In fact, there is considerable risk that between now and the time when Congress adjourns in November or December, it will take actions that *increase* mid-term and long-term deficits (through tax-cutting measures that cost more than its program cuts save) while making the lives of millions of the nation's poorest citizens harsher. Such a course of action would be doubly unfortunate.

But there is still the possibility for the current focus on hurricane-related costs to provide an impetus for policymakers to start, at long last, taking steps to address the nation's troubled fiscal outlook. This analysis suggests a series of balanced initial steps, involving both spending and revenues, that policymakers could take to stop digging the hole deeper and start making progress in closing the fiscal gap. These proposals represent only first steps. Much larger actions on both the program and revenue sides of the budget ultimately will be necessary.

[12] Robert M. Ball, "How to Fix Social Security?" *Aging Today*, March-April, 2004.

**Congressman John Shadegg Testimony**

*Subcommittee on Federal Financial Management, Government Information, and International Security*

**October 25, 2005**

Thank you, Mr. Chairman, for allowing me to testify on the importance of the Tenth Amendment and a bill I introduced to protect it, the Enumerated Powers Act.

The Tenth Amendment to the United States Constitution reads as follows:
*"The powers not delegated to the United States by Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people"*

In other words, the national government cannot expand its legislative authority into areas reserved to the States or the people. As the final amendment in the Bill of Rights, the Tenth Amendment makes it clear that that the Constitution establishes a federal government of delegated, enumerated, and thus *limited* powers.

For that reason, every Congress since the 104$^{th}$ Congress I have introduced the Enumerated Powers Act. This legislation requires that all bills introduced in the U.S. Congress contain a statement setting forth the specific constitutional authority pursuant to which the law is being enacted. This measure will force a constant and ongoing reexamination of the role of the national government. The Enumerated Powers bill is a simple measure, but it is intended to require scrutiny that should fundamentally slow the ever-growing reach of the federal government. It will perform three important functions:

First, this legislation will encourage members of Congress to pause, reflect, and debate where a proposed piece of legislation fits within the Constitutional allocation of powers between the federal government, states, and the people.

The Supreme Court has confirmed the importance of the Tenth Amendment in decisions this decade. In the 1996 case, *United States v. Lopez*, the Supreme Court ruled Congress did not have the authority to require gun-free school zones. Apart from the question of whether such zones are a good idea, Congress simply lacks the power under the Constitution to mandate them. In this case, the Court determined that even the interstate commerce clause, used so often in the past as a blank check for federal action, did not apply because gun-free school zones had nothing to do with interstate commerce. Justice Kennedy concurred in the opinion:

*It would be mistaken and mischievous for the political branches to forget that the sworn obligation to preserve and protect the Constitution in maintaining the federal balance is their own in the first and primary instance.*

The second function of the Enumerated Powers Act would be to include a statement of the Constitutional authority pursuant to which Congress is acting, which will put Congress's view on record for the people to judge. The constitutional authority must be written in the bill itself.

Finally, such a statement will assist the courts in evaluating the constitutionality of the legislation enacted. Legislation that falls within our enumerated powers will more likely be upheld if it contains an explicit explanation of its constitutional basis. And if the statement of Constitutional authority does not stand up to scrutiny, both the courts and the people will find it easier to hold Congress accountable.

Let me describe for you what "explicit explanation" means. On far too many occasions, committee reports come through Congress citing the General Welfare Clause, the necessary and proper clause, or, even more broadly Article I, Section 8 – the entire Powers of Congress section. House Rule XIII, Section 3(d) (1) requires that all committee reports contain "a statement citing the specific powers granted to Congress in the Constitution to enact the law proposed by the bill or joint resolution." The key word here is "specific," yet too often, our committees fail to cite specific constitutional authority.

This House Rule was actually enacted at the beginning of the 105th Congress. That Congress incorporated the substantive requirement of my bill into House rules by requiring that report language must cite constitutional authority. However, the full effect of the Enumerated Powers Act will not be realized until it is incorporated into the bill itself and into actual law.

History of the Principle of Federalism

In 1787, when the Founding Fathers wrote our Constitution, they created a national government with far-reaching but limited powers. They believed that granting specific, rather than general, legislative powers to the national government would be one of the central mechanisms for protecting our freedoms while allowing us to achieve the objectives best accomplished through a national government. As a result, the Constitution gives the federal government only eighteen specific enumerated powers.

Federalism invests two separate levels of government with jurisdiction over the same territory and the same citizens, as explained in Federalist Number 51. The Founders envisioned a form that would enable government to control the governed and also oblige the government to control itself. Federalism is intended as a constraint on government.

To our Founding Fathers, government presented a monopoly problem and the way to deal with it was to limit the central government's authority to a sphere of enumerated powers. In all those areas beyond Congress's purview, the Founder's sought to force the states to compete for their citizens' business, labor, and capital. The be-all and end-all of federalism is the doctrine of enumerated powers. Without that doctrine, Congress could pass any law at all. It could establish state uniform national rules on any subject and bypass the Founder's goal of state competition and experimentation.

For the longest part of our history, the first 150 years, from 1787 to 1937, the national government was a bulwark against excessive federal regulation. Unfortunately, the restraint demonstrated by the early Congresses was largely abandoned in the latter part of the twentieth century, and now in the twenty-first century. Beginning with the New Deal era, modern Congresses have displayed a willingness to pass any kind of law they want.

Virtually all of these laws, from labor and civil rights measures to environmental protection and crime control, are well-intentioned. But from a constitutional perspective, Congress does not possess the authority to enact many of them. The federal government has ignored the Constitution and expanded its authority into every aspect of human conduct. State governments and individual citizens have been denied their rightful – and lawful – role in our system of government.

The size and scope of the national government has exploded over the past seven decades, and many doubt the remaining vitality of this central feature of our Constitution. Yet the belief that the central government should have only limited powers remains alive in the hearts of Americans who believe that people, not government programs, hold the answers to our nation's problems.

Consider these bills: the UN Reform Act, the Water Resources Development Act, the Vocational and Technical Education for the Future Act, and even the Charles 'Pete' Conrad Astronomy Awards Act. These are just a few examples of the many bills passed by the House during the $109^{th}$ Congress that do not cite specific constitutional authority in the committee report. Countless others have been introduced with the same problem. This is unacceptable.

For too long, the federal government has operated without constitutional restraint, blatantly ignoring the principles of federalism. In so doing, it has created ineffective and costly programs, massive deficits year after year, and a national debt totaling approximately $8 trillion and rising. The Enumerated Powers Act will help slow the flood of unconstitutional legislation while assisting Congress in its ongoing reexamination of the proper role of the federal government.

Right now, we have an opportunity to cut back on some of these ineffective programs and projects taken on by the federal government. In the wake of Hurricane Katrina, and at a time when federal spending has ballooned to an unsustainable level, two things need to be achieved: 1.) We need to cut back on some of the spending that occurs in Washington on projects wrongfully taken on by the federal government and 2.) We need to implement a system in which Congress reflects upon how proposed legislation fits into the federalist scheme.

Today, many Americans not only expect government to solve their problems, but believe that government has all-but-unlimited authority to do so. I became a member of Congress because I wanted to shrink the size and scope of the federal government and return power to the American people, as our forefathers envisioned. One of the most important things Congress can do is to honor and abide by the principles embodied in the Constitution – no more, no less. Respecting the Tenth Amendment is the first way to ensure that the genius of the Constitution and its division of power between the national government, the states, and the people continues to guide our nation.

As Barry Goldwater wrote in *The Conscience of a Conservative*:

"I have little interest in streamlining government or in making it more efficient, for I mean to reduce its size. I do not undertake to promote welfare, for I propose to extend freedom.

My aim is not to pass laws, but to repeal them. It is not to inaugurate new programs, but to cancel old ones that do violence to the Constitution, or that have failed in their purpose, or that impose on the people an unwarranted financial burden. I will not attempt to discover whether legislation is 'needed' before I have first determined whether it is constitutionally permissible. And if I should later be attacked for neglecting my constituents' interests, I shall reply that I was informed their main interest is liberty and that in that cause I am doing the very best I can."

Again, thank you, Mr. Chairman, for allowing me to testify today.

**COMMITTEE HEARING**

**October 25, 2005**

**Guns & Butter: Setting Priorities in Federal Spending in the Context of Natural Disaster, Deficits and War**

**Testimony of Charlie Stenholm,**
**Government Affairs Advisor of Olsson, Frank and Weeda, P.C**

**And Former Member of Congress**

Mr. Chairman, Senator Carper and Members of the Committee. I am Charlie Stenholm, a former Member of Congress from the 17th District of Texas and currently a Government Affairs Advisor at Olsson, Frank and Weeda. I am also a member of the Board of Directors of the Committee for a Responsible Federal Budget and the Concord Coalition. This testimony is my own and does not represent any position or conclusion of any of these organizations.

In my twenty-six years in Congress, I worked with many members on both sides of the aisle, including several members of this committee, fighting to leave a better future for our children and grandchildren. We spent many years working extremely hard and casting many tough votes to eliminate the deficit and put us in a position to begin paying down the debt. It pains me to see that so much of that hard work has been squandered.

It has been encouraging over the last few weeks to hear the "deficits don't matter" rhetoric of the last few years be replaced by expressions of concern about deficit spending. As a long-time advocate of pay as you go budgeting, it is heartening to hear talk about offsetting the costs of legislation to prevent the deficit from increasing. Unfortunately, the leadership in Congress didn't rediscover the common sense principle of pay as you go until after enacting legislation adding several trillion dollars to our nation's debt. Even now, the leadership continues to apply this principle selectively, focusing exclusively on spending to assist people harmed by Hurricane Katrina while continuing to refuse to acknowledge and offset the costs of tax cuts.

I applaud efforts to find offsets for the costs of disaster relief in the Gulf Coast. However, it is far more important that Congress offset the costs of legislation that will have a permanent impact on the long-term budget outlook. Focusing on offsetting the one-time, temporary costs of disaster relief while ignoring the costs of legislation that will permanently increase the deficit by a much greater amount over the long term makes no sense.

I would like to believe that the leadership in Congress has undergone a conversion on the road to Damascus in fiscal policy. But the refusal to reconsider legislation enacted over the last several years which has led to our current deficit situation and insistence on moving forward with tax cuts and other legislation that would increase the deficit casts doubts on the seriousness of their newfound concern for the deficit.

Over the years I regularly stood up and criticized my party for being fiscally irresponsible. I am proud that my party has come to recognize the damage that deficit spending does to the values we care about and now stands for fiscal responsibility. I regret that, over the past decade, Republican leaders in Washington who used to agree with me about the importance of fiscal discipline apparently abandoned their belief in the value of balancing our budget.

**From Deficits to Surpluses and Back**

In the 1990s, a bipartisan consensus in Congress recognized that we could not continue to allow deficits and debt to spiral out of control. We balanced the budget, and the benefits were enormous: the longest peacetime expansion of the American economy in 50 years, four straight years of budget surpluses, record low unemployment and poverty rates, and record high homeownership. In January of 2001, the Congressional Budget Office projected a budget surplus of $5.6 trillion over ten years. We were on path to paying off the publicly held debt. There were even warnings that we were in danger of paying off debt too quickly.

Today, our nation has returned to the era of deficits as far as the eye can see. Just last week, the national debt broke through the $8 trillion barrier, a number that seemed incomprehensible just a few short years ago. The national debt is on track to exceed $10 trillion in debt by 2008 or early 2009. Earlier this year, the Congressional Budget Office estimated that the policies in the budget submitted by the President would produce deficits of $1.765 trillion over the next five years. When the CBO's projections of deficits under the President's policies are combined with the actual deficits of the last four years, total deficits will be more than $9 trillion higher over the ten year period than CBO had projected in 2001.

It is true that our nation has faced unexpected emergencies that have contributed to the deficit, but that is not an excuse for running deficits. Many of us warned that the anticipated budget surpluses were only projections and that it was dangerous to make commitments using all of the projected surpluses without leaving any room for error. We warned that if the projections didn't turn out exactly as hoped, we would return to deficits.

While nobody could have predicted 9-11, hurricane Katrina or the other crises our nation has faced over the last several years that have had an impact on the budget, it was irresponsible to assume that we wouldn't face any unanticipated circumstances when we decided to use all of the projected surplus for tax cuts. We should have set aside some of the projected surplus as a cushion to prepare for unanticipated costs. And when we were faced with those unanticipated costs, we should have gone back and made changes in our budget plans. But instead we simply added those costs on top of the costs of legislation that was enacted when we had projected surpluses.

**Deficits Do Matter**

Defenders of our current economic and fiscal policies have argued that deficits don't matter. The reality is that deficits do matter, both for our economic security today as well as the future we leave for our children and grandchildren.

The United States has been able to sustain large budget deficits without an increase in domestic interest rates because the increased demand for borrowing has been offset by an increased inflow of capital from global markets. While this inflow of foreign capital helps keep interest rates down in the short term, it creates mortgages on future national income that has to be siphoned off to repay foreign investors who financed government deficits. This will give foreign investors a greater claim on future economic resources provided by American workers. Our increased reliance on foreign capital to finance our deficits places our economic security at the mercy of global bankers and foreign governments. If foreign investors stop buying US bonds we would face higher inflation and higher interest rates, putting our economy at risk of a large scale recession.

Large deficits financed by borrowing from foreign investors are also a major factor contributing to the trade deficits which are exporting jobs overseas. We need to keep the value of the dollar high in order to attract the foreign capital we need to finance our debt. If the value of the dollar declines, US bonds will be less valuable to foreign investors. But the strong dollar we need to help Treasury finance our budget deficits hurts our businesses by making US exports more expensive.

Budget deficits place a drag on the economy and our living standards now and in the future. Federal Reserve Chairman Alan Greenspan has repeatedly warned that deficits undercut the ability of the economy to grow in a way that reduces unemployment and increases the wages of American workers.

The $352 billion we spent last year for interest on our $6.7 trillion national debt represents a "debt tax" that must be paid by all future generations and can never be repealed. The best way to ensure that we, as well as our children and our grandchildren, are overtaxed for the rest of our lives is to keep borrowing money. Any benefits to families today from tax cuts will be outweighed by the debt burden that will be placed on families today and in the future.

Our current borrow and spend policies are worse than the tax and spend policies of the past, because they will leave a crushing debt tax burden for future generations who don't have any say in what we are doing and don't benefit from the tax cuts and spending programs for current generations.

A German philosopher named Dietrich Bonhoeffer once said that the ultimate test of a moral society is the kind of world that it leaves to its children. We cannot leave it to our grandchildren to shoulder the enormous burden of our debt.

Our grandchildren will face ever higher tax burdens simply to cover increasing interest payments instead of addressing other needs such as keeping our military the strongest in the world, protecting our domestic security, providing health care, strengthening Social Security and Medicare, and investing in our education system.

Our grandchildren do not have a vote. That is why it is so easy for us to say here today we can fight two wars, we can fund homeland security, we can fight the war on terrorism, we can rebuild the Gulf Coast and we can keep cutting taxes, because we are going to send the bill to our grandchildren.

One of my proudest moments in Congress was when the House passed the Balanced Budget Amendment to the Constitution, and one of my greatest disappointments was when the Senate fell one vote short of approving it. A Balanced Budget Constitutional Amendment and strong budget enforcement rules would protect the rights of future generations who are not represented in our political system but will bear the burden of our decisions today. If a Balanced Budget Amendment were already in the Constitution, we would not have been able to enact the budget policies advocated by the majority that have resulted in a rapid increase in our national debt.

Balancing the budget will require bipartisan cooperation, as we did in 1997. A serious discussion about balancing the budget will require both parties to make sacrifices. All areas of the budget must be on the table and the burden of deficit reduction should be distributed fairly across the budget. I have always said that those of us in agriculture are willing to accept our fair share of reductions if all other areas of the budget are asked to sacrifice as well, but we aren't willing to shoulder an undue burden of cuts so that other areas of the budget can avoid budget discipline. I believe that this view is shared by advocates of other areas of the budget as well.

It is neither fiscally responsible nor politically viable to make cutbacks in some areas of the budget in the name of deficit reduction while exempting other areas of the budget from budget discipline and going forward with other proposals which would increase the deficit. That is particularly true when deficit reduction efforts focus on the most vulnerable in society, while benefits for those in a better position to accept sacrifices are left untouched. It will take everyone pulling to get the wagon out of the ditch; we won't be able to get it out if some people are riding.

**The First Step Toward Getting Out Of The Deficit Hole: Quit Digging**

The first step in bringing the deficit under control is to stop digging the hole deeper with tax cuts financed with borrowed money. Rhetoric about controlling the deficit by offsetting increased spending doesn't have much credibility when Congress continues to go forward with plans to enact additional tax cuts

The budget resolution adopted by Congress would allow for an increase in the deficit of $166 billion over the next five years because the tax cuts as well as increased spending for defense and homeland security would dwarf the cuts in domestic spending programs. While there has been a great deal of attention in recent weeks to the $35 billion in entitlement savings required by the budget resolution, it also allows for tax cuts of $106 billion, including $70 billion under fast-track reconciliation procedures that were originally intended to facilitate passage of politically difficult deficit reduction legislation.

We have now enacted three tax cuts based on the theory that tax cuts will stimulate the economy and pay for themselves as a result of economic growth. In 2001, Congress passed a tax cut proposed by President Bush that was described as insurance against an economic downturn. In 2002, we enacted another tax cut as an economic stimulus. In 2003 we passed yet another tax cut that in the name of promoting economic growth plan. Each time advocates of the tax cuts dismissed warnings about the impact on the deficit, yet the deficit continued to grow.

No reputable analyst believes that cutting taxes will result in higher revenues than would have occurred without the tax cut. While some tax cuts may result in economic growth that produces some feedback, there is no credible analysis that claims those potential benefits would offset the revenue. Analyses from the Congressional Budget Office, the Joint Committee on Taxation, the Federal Reserve Board, and others have all concluded that the tax cuts enacted over the last four years will have little or no impact on long term economic growth, and result in deficits larger than they otherwise would have been. Even the President's own economic advisors have stated that there is no evidence that the tax cuts will pay for themselves and increase revenues.

Although some advocates of tax cuts have claimed that recent reports showing higher-than-expected revenue collections last year is evidence that the fiscal policies of the last five years are working, the reality is that the recent increase in revenues just partially begins to restore the decline in revenues over the last several years. The recent increase in revenues follows three consecutive years (2001-2003) in which revenues declined in nominal terms.

Even with the unexpected increase in revenues last year, actual revenues in fiscal year 2005 are more than $230 billion lower than they were projected to be in 2001 after taking into account the costs of the 2001 and 2003 tax cuts under so-called "static scoring". There are many reasons that actual revenues have been much lower than Congress and the administration projected when the tax cuts were enacted, but clearly those tax cuts have not paid for themselves by boosting revenues.

**Returning To What Has Worked: Reinstate Paygo Budget Enforcement Rules**

Any serious effort to restore fiscal discipline should begin with reinstating the pay as you go budget enforcement rules and discretionary spending limits restricting the ability of Congress and the President to enact legislation that would increase the deficit. These budget enforcement rules, which Congress and the President enacted in 1990 and extended in 1997 with bipartisan support, were an important part of getting a handle on the deficits in the early 1990s and getting the budget back into balance. Reinstating paygo rules would not by itself balance the budget, but it would represent an important first step in bringing discipline to the budget process by prohibiting policy changes that would further enlarge the deficit.

The principle of paygo -- if we want to reduce our revenues or increase our spending, we need to say how we would pay for it within our budget – is something all families understand. If we want to reduce our revenues, we need to say what spending we will do without. If we want to increase spending, we need to say where we will come up with the revenues for the new spending or what other spending we will do without.

I would say with all due respect to my Republican friends that if you are sincere in what say about controlling spending, you should not have a problem with reinstating pay as you go for taxes as well as spending because it would force Congress to actually cut spending to accompany tax cuts instead of just promising to cut spending in the future. The problem is that the actions of the majority in Congress haven't matched their rhetoric. Congress and the administration have cut taxes without cutting spending, and have charged the difference to our children and grandchildren by increasing the deficit.

**Eliminating Low-priority and Unnecessary Spending**

One small step that would help restore a small measure of fiscal discipline is enactment of expedited rescission legislation that strengthen the ability of Presidents to identify and eliminate wasteful or low-priority spending items. Expedited rescission legislation embodies an idea which many Members, both Democrats and Republicans, have advocated for years. Senator Carper was an early leader on this issue, working with Dick Armey, Tim Johnson and others to find a bipartisan consensus on this issue.

Expedited rescission legislation would bring greater accountability to the appropriations process so that individual appropriations may be considered on their individual merits. The current rescission process does not make the President or Congress accountable. Congress can ignore the President's rescissions, and the President can blame Congress for ignoring his rescissions. I believe that it is appropriate to strengthen the President's ability to force votes on individual budgetary items. It will not make a significant dent in our deficit. But it will have a very real cleansing effect on the legislative process and will take a step toward reducing the public cynicism about the political process.

Expedited rescission authority can be an important tool for eliminating wasteful spending, if the President uses this tool. I have been disappointed that President Bush has not exercised his authority under current law to send Congress a rescission list of low-priority spending and pork barrel projects that he wants Congress to eliminate. I would encourage the President to make use of his rescission authority whether or not Congress enacts expedited rescission.

Another tool that Congress should consider to eliminate low-priority spending is sunset legislation to provide for a regular review of the efficiency and public need every federal agency, department and program. This would require agencies to justify their existence to taxpayers and Congress and provide an opportunity for Congress to consider changes in operations of an agency and the programs it administers, create new efficiencies, and eliminate obsolete programs or offices.

Not only would sunset legislation provide for abolishment of obsolete federal agencies and streamline others, it would encourage Congress as well as agencies to look for ways to improve programs to better serve taxpayers. A similar law is used in nearly half of the states including Texas, which has eliminated 44 agencies, saving Texas taxpayers $720 million.

**Improving Accuracy of Indexation for Government Programs**

One specific proposal that would provide a substantial source of savings I would encourage the Committee to consider is utilizing a more accurate measure for indexing government programs as well as tax brackets and other provisions in the tax code. There is broad agreement among economists that the Consumer Price Index currently used for indexation of government programs overstates inflation. The Bureau of Labor Statistics has begun to publish a new "Chained Consumer Price Index", also known as a superlative index to eliminate the upper level substitution bias in the CPI. BLS has estimated that the Chained CPI will grow about 0.2 percentage points slower than the customary CPI

Using the Chained CPI for indexation of government programs represents sound policy that reflects years of work by economists and other technical experts. Just as importantly, this proposal would achieve substantial budgetary savings – approximately $50 billion over the next five years -- in a way which would spread the burden of deficit reduction fairly across the entire span of government.

### Addressing Long-Term Fiscal Problems

While looking for savings to offset the costs for Katrina and address our short term deficit situation, it is even more important that we address the larger budget challenges over the long term, particularly with regard to Social Security and Medicare. I had hoped that this would be the year that Congress and the President would take action to address the financial challenges facing Social Security, but neither party seemed interested in a serious discussion about the tough choices that will be necessary. These challenges will continue to get worse and become harder to address the longer we wait. And as we all know, the challenges facing Medicare and Medicaid are even greater.

Finding a politically viable and equitable solution to these challenges will require bipartisan discussions in which all options are on the table for consideration and there are no preconditions by either side about what must be included or excluded from a final solution. I have come to the conclusion that we should seriously consider proposals to establish a bipartisan commission to objectively review all the options for reforms of our entitlement programs and make recommendations.

### Reaching a Bipartisan Consensus on a Responsible Plan to Restore Fiscal Discipline

There is no shortage of options for Congress to consider as part of a plan to bring the deficit under control. I have attached an op-chart published in the New York Times by Maya MacGuineas, President of the Committee for a Responsible Federal Budget, as well as suggestions put forward by the Concord Coalition and the Center for Budget and Policy Priorities. That there is a substantial degree of overlap in the suggestions made by these organizations gives me reason to believe that we could reach broad agreement on a plan to restore fiscal discipline and bring the deficit under control if everyone is willing to come to the table and seriously consider all options for savings.

While each of us may disagree with some of the individual items suggested, all of us must be willing to accept sacrifices in areas we support in order to reach a consensus on a balanced package. As long as everyone advocates balancing the budget by cutting someone else's priorities, talk about deficit reduction will remain just that. As a farmer, I choose to be an optimist and believe that all sides will be willing to put aside their individual political interests to find a solution that is in the best interests of our nation and our children's future.

**STATEMENT**

**of**

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**before the**

**Committee on Homeland Security and Governmental Affairs**
**Subcommittee on Federal Financial Management, Government Information, and International Security**

**October 25, 2005**

**RE: Guns and Butter: Setting Priorities in Federal Spending in the Context of Natural Disasters, Deficits, and War**

Mr. Chairman, distinguished members of the subcommittee:

My name is Roger Pilon. I am vice president for legal affairs at the Cato Institute and director of Cato's Center for Constitutional Studies.[1] I want to thank you, Mr. Chairman, for inviting me to testify today on "Guns and Butter: Setting Priorities in Federal Spending in the Context of Natural Disasters, Deficits, and War"—the purpose of the hearing being, as your letter of invitation states, "to focus on the limits and role of our federal government as outlined in the Constitution."

I can well understand your concern to focus on that issue, Mr. Chairman. In *Federalist* 45, James Madison, the principal author of the Constitution, spoke to a skeptical nation, worried that the document the Constitutional Convention had just drafted gave the central government too much power. Be assured, he said, the powers of the new government were, and I quote, "few and defined." How things have changed. Yet in its 218 years, the Constitution itself has changed very little. The questions before us, then, are (1) under that Constitution, how did we go from limited to essentially unlimited government, (2) what are the implications, and (3) what should be done about it?

A closely related question is whether Madison understood and correctly reported on the document he'd just drafted, or whether modern interpretations of the Constitution, which have allowed our modern Leviathan to arise, are correct. Let me say here that Madison was right; the modern interpretations are wrong. As a corollary, most of what

[1] A biographical sketch is attached.

the federal government is doing today is unconstitutional because done without constitutional authority. That contention will doubtless surprise many, but there you have it. I mean to speak plainly in this testimony and call things by their proper name.

But before I defend that contention by addressing those questions, let me note that the nominal subject of these hearings—"setting priorities in federal spending"—concerns mainly a matter of policy, not law. Unless some law otherwise addresses it, that is, how Congress prioritizes its spending is its and the people's business—a political matter. By contrast, the subtext of these hearings, which I gather is the subcommittee's principal concern, is "the limits and role of our federal government as outlined in the Constitution," and that is mainly a legal question. I distinguish those questions, let me be clear, for a very important reason. It is because we live under a Constitution that establishes the rules for legitimacy. Thus, in the case at hand, Congress may have pressing policy reasons for prioritizing spending in a given way, but such reasons are irrelevant to the question of whether that spending is constitutional.

**Constitutional Legitimacy**

Because that distinction and the underlying issue of legitimacy are so central to these hearings, they warrant further elaboration at the outset. In brief, our Constitution serves four main functions: to authorize, institute, empower, and limit the federal government. Ratification accomplished those ends, lending political and legal legitimacy to institutions and powers that purported by and large to be morally legitimate because grounded in reason. Taken together, the Preamble, the first sentence of Article I, the inherent structure of the document, and especially the Tenth Amendment indicate that ours is a government of delegated, enumerated, and thus limited powers. The Constitution's theory of legitimacy is thus simple and straightforward: To be legitimate, a power must first have been delegated by the people, as evidenced by its enumeration in the Constitution. That is the doctrine of enumerated powers, the centerpiece of the Constitution. For the Framers, it was the main restraint against overweening government. In fact, the Bill of Rights, which we think of today as the main restraint, was an afterthought, added two years later for extra precaution.

Once that fundamental principle is grasped, a second follows: Federal powers can be expanded only by constitutional amendment, not by transient electoral or congressional majorities. Over the years, however, few such amendments have been added. In the main, therefore, Article I, section 8 enumerates the 18 basic powers of Congress—the power to tax, the power to borrow, the power to regulate commerce with foreign nations and among the states, and so forth, concluding with the power to enact such laws as may be necessary and proper for executing the government's other enumerated powers. It is a short list, the idea being, as the Tenth Amendment makes explicit and the *Federalist* explains, that most power is to remain with the states—or with the people, never having been delegated to either level of government.[2]

[2] The Tenth Amendment states: "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people."

In fact, given the paucity and character of the federal government's enumerated powers, it is plain that the Framers meant for most of life to be lived in the private sector—beyond the reach of politics, yet under the rule of law—with governments at all levels doing only what they have been authorized to do. Far from authorizing the ubiquitous government planning and programs we have today, the Constitution allows only limited government, dedicated primarily to securing the conditions of liberty that enable people to plan and live their own lives. I turn, then, to the first of the questions set forth above: How did we move from a Constitution that limited government to one that is read today to authorize effectively unlimited government?

**From Limited to Unlimited Government**

The great constitutional change took place in 1937 and 1938, during the New Deal, all without benefit of constitutional amendment; but the seeds for that change had been sown well before that, during the Progressive Era.[3] Before examining that transition, however, I want to lay a proper foundation by sketching briefly how earlier generations had largely resisted the inevitable pressures to expand government. It is an inspiring story, told best, I have found, in a thin volume written in 1932 by Professor Charles Warren of the Harvard Law School. Aptly titled, *Congress as Santa Claus: or National Donations and the General Welfare Clause of the Constitution*, this little book documents our slow slide from liberty and limited government to the welfare state—and that was 1932! In truth, however, Warren's despair over that slide notwithstanding, the book is a wonderful account of just how long we lived under the original design, for the most part, before things started to fall apart during the Progressive Era. And so I will share with the subcommittee just a few snippets and themes from the book, along with material from other sources, to convey something of a sense of how things have changed—not only in the law but, more important, in the culture, in our attitude toward the law.

When Thomas Jefferson wrote that it was the natural tendency for government to grow and liberty to yield, he doubtless had in mind his rival, Alexander Hamilton, for hardly had the new government begun to operate when Hamilton proposed a national industrial policy in his 1791 *Report on Manufactures*.[4] To Hamilton's argument that Congress had the power to pronounce upon the objects that concern the general welfare and that these objects extended to "the general interests of learning, of agriculture, of manufacturing, and of commerce,"[5] Madison responded sharply that "the federal Government has been hitherto limited to the specified powers, by the Greatest Champions for Latitude in expounding those powers. If not only the *means*, but the

[3] For a discussion of the Progressives' approach to the Constitution, see Richard A. Epstein, "The Monopolistic Vices of Progressive Constitutionalism, 2004-2005 Cato Sup. Ct. Rev. 11 (2005); Richard A. Epstein, How Progressives Rewrote the Constitution (2006) (forthcoming).

[4] See Arthur Harrison Cole ed., Industrial and Commercial Correspondence of Alexander Hamilton 247 (1968).

[5] Id.

*objects* are unlimited, the parchment had better be thrown into the fire at once."[6] Congress shelved Hamilton's *Report*. He lost that battle, but over time he won the war.

The early years saw numerous attempts to expand government's powers, but the resistance mostly held. In 1794, for example, a bill was introduced in the House to appropriate $15,000 for the relief of French refugees who had fled to Baltimore and Philadelphia from an insurrection in San Domingo,[7] whereupon Madison rose on the floor to say that he could not "undertake to lay [his] finger on that article of the Federal Constitution which granted a right to Congress of expending, on objects of benevolence, the money of their constituents."[8] Two years later a similar bill, for relief of Savannah fire victims, was defeated decisively, a majority in Congress finding that the General Welfare Clause afforded no authority for so particular an appropriation.[9] As Virginia's William B. Giles observed, "[The House] should not attend to what ... generosity and humanity required, but what the Constitution and their duty required."[10]

Those early attempts to expand Congress's power, and the resistance to them, centered on the so-called General Welfare Clause of the Constitution, found in the first of Congress's 18 enumerated powers.[11] Hamilton argued that the clause authorized Congress to tax and spend for the general welfare. Not so, said Madison, Jefferson, and many others. South Carolina's William Drayton put it best in 1828:

> If Congress can determine what constitutes the General Welfare and can appropriate money for its advancement, where is the limitation to carrying into execution whatever can be effected by money? How few objects are there which money cannot accomplish! ... Can it be conceived that the great and wise men who devised our Constitution ... should have failed so egregiously ... as to grant a power which rendered restriction upon power practically unavailing?[12]

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[6] Letter to Henry Lee, in 6 The Writings of James Madison, at 81n. (Gaillard Hunt ed., 1906) (original emphasis).
[7] Act of Feb. 12, 1794, 6 Stat. 13.
[8] 4 Annals of Cong. 170 (1794).
[9] 6 Annals of Cong. 1727 (1796).
[10] Id. at 1724.
[11] "The Congress shall have Power To lay and collect Taxes, Imposts and Excises, to pay the Debts and provide for the common Defense and General Welfare of the United States; . . . ."
[12] 4 Reg. Deb. 1632-34 (1828). Madison made a similar point on several occasions. See, e.g., James Madison, "Report on Resolutions," in 6 *The Writings of James Madison* 357 (Gaillard Hunt ed., 1900): "Money cannot be applied to the *general welfare*, otherwise than by an application of it to some *particular* measure conducive to the general welfare. Whenever, therefore, money has been raised by the general authority, and is to be applied to a particular measure, a question arises whether the particular measure be within the enumerated authorities vested in Congress. If it be, the money requisite for it may be applied to it; if it be not, no such application can be made." (emphasis in original). And Jefferson also addressed the issue. See, e.g., "Letter from Thomas Jefferson to Albert Gallatin" (June 16, 1817) in *Writings of Thomas Jefferson* 91 (Paul Leicester Ford ed., 1899): "[O]ur tenet ever was, and, indeed, it is almost the only landmark which now divides the federalists from the republicans, that Congress had not unlimited powers to provide for the general welfare, but were restrained to those specifically enumerated; and that, as it was never meant they should . . . raise money for purposes which the enumeration did not place under their action; consequently, that the specification of powers is a limitation of the purpose for which they may raise money."

Stated differently—with reference to constitutional structure—what was the point of enumerating Congress's powers if any time it wanted to do something it was not authorized to do, because there was no power granted to do it, Congress could simply say it was spending for the "general welfare" and thus make an end-run around the limits imposed by the doctrine of enumerated powers? Enumeration would have been pointless.

That argument largely held through the course of the 19th century. To be sure, inroads on limited government were made on other constitutional grounds, as Warren recounts. Congress made gifts of land held in trust under the Public Lands Clause, for example, with dubious consideration given in return; then gifts of revenues from the sale of such lands; and finally, gifts of tax revenues generally.[13] But there were also numerous examples of resistance to such redistributive schemes. Thus, in 1887, 100 years after the Constitution was written, President Grover Cleveland vetoed a bill appropriating $10,000 for distribution of seeds to Texas farmers suffering from a drought.[14] In his veto message he put it plainly: "I can find no warrant for such an appropriation in the Constitution."[15] Congress sustained the veto. And as late as 1907 we find the Supreme Court expressly upholding the doctrine of enumerated powers in *Kansas v. Colorado*:

> The proposition that there are legislative powers affecting the Nation as a whole which belong to, although not expressed in [,] the grant of powers, is in direct conflict with the doctrine that this is a government of enumerated powers. ... The natural construction of the original body of the Constitution is made absolutely certain by the Tenth Amendment.[16]

Thus, although the doctrine of enumerated powers faced political pressure from the start, and increasing pressure as time went on, the pattern we see through our first 150 years under the Constitution can be summed up as follows. In the early years, measures to expand government's powers beyond those enumerated in the Constitution rarely got out of Congress because they were stopped by objections in that branch—*constitutional* objections. Members of Congress actually debated whether they had the power to do whatever it was that was being proposed; they didn't simply assume they had the power and then leave it to the courts to check them. *Congress took the Constitution and the limits it imposed on congressional action seriously.*[17] Then when constitutionally dubious bills did get out of Congress, presidents vetoed them—not simply on policy but on *constitutional* grounds. And finally, when that brake failed, the Court stepped in. In short, the system of checks and balances worked because the Constitution was taken seriously by sufficient numbers of those who had sworn to uphold it.

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[13] Charles Warren, Congress as Santa Claus 32 (1932).
[14] H.R. 10203, 49th Cong., 2d Sess. (1887).
[15] 18 Cong. Rec. 1875 (1887).
[16] Kansas v. Colorado 206 U.S. 46, 89 (1907).
[17] Contrast that with Congress's enactment of the Gun-Free Schools Act of 1990 (18 U.S.C. § 922 (q)(1)(A) (1988 ed., Supp. V), which the Court found unconstitutional in 1995, holding for the first time in nearly 60 years that Congress had exceeded its authority under the Commerce Clause. United States v. Lopez, 514 U.S. 549 (1995). In enacting the statute, Congress had not even bothered to cite its constitutional authority for doing so.

The Progressive Era called all of that into question. Marked by a fundamental change in the climate of ideas, it paved the way for the New Deal. In fact, as early as 1900 we could find *The Nation*, before it became an instrument of the modern left, lamenting the demise of classical liberalism. In an editorial entitled "The Eclipse of Liberalism," the magazine's editors surveyed the European scene, then wrote that in America, too, "recent events show how much ground has been lost. The Declaration of Independence no longer arouses enthusiasm; it is an embarrassing instrument which requires to be explained away. The Constitution is said to be 'outgrown.'"[18]

The Progressives to whom those editors were pointing, sequestered often in elite universities of the East, were animated by ideas from abroad: British utilitarianism, which had supplanted the natural rights theory on which the Constitution rested; German theories about good government, as reflected in Chancellor Otto von Bismarck's social security experiment; plus our own homegrown theories about democracy and pragmatism.[19] Combined with the emerging social sciences, those forces constituted a heady brew that nourished grand ideas about the role government could play in improving the human condition. No longer viewing government as a necessary evil, as the Founders had, Progressives saw the state as an engine of good, an instrument through which to solve all manner of social and economic problems. In a word, it was to be better living through bigger government.[20]

But a serious obstacle confronted the political activists of the Progressive Era—that troublesome Constitution and the willingness of judges to enforce it. Dedicated to liberty and limited government, and hostile to government planning garbed even in "the public good," the Constitution stood as a bulwark against overweening government, much as the Framers intended it would. Not always,[21] to be sure, but for the most part.

With the onset of the New Deal, however, Progressives shifted the focus of their activism from the state to the federal level. But they fared little better there as the Court found several of President Franklin Roosevelt's schemes unconstitutional, holding that Congress had no authority to enact them.[22] Not surprisingly, that prompted intense debate

[18] The Nation, Aug. 9, 1900, p. 105.
[19] See Robert S. Summers, Pragmatic Instrumentalism: America's Leading Theory of Law, 5 Cornell L. F. 15 (1978).
[20] Progressives did not limit their attention to economic regulation. In 1927, for example, we find Justice Oliver Wendell Holmes, the "Yankee from Olympus," writing for the Court to uphold a Virginia statute that authorized the sterilization of people thought to be of insufficient intelligence. Buck v. Bell, 274 U.S. 200 (1927). There followed in this country some 70,000 sterilizations. For an insightful discussion of the case and surrounding issues, see William E. Leuchtenburg, Mr. Justice Holmes and Three Generations of Imbeciles, ch. 1 in The Supreme Court Reborn: The Constitutional Revolution in the Age of Roosevelt (1995).
[21] *Buck v. Bell*, *supra* note 20, is a good example, as is *Euclid v. Ambler Realty*, 272 U.S. 365 (1926), which upheld a zoning ordinance involving a regulatory taking of property without compensation.
[22] Thus, on "Black Monday," May 27, 1935, in three 9-0 decisions, the Court invalidated the National Industrial Recovery Act and the Frazier-Lemke Act on mortgage moratoria and, in *Humphrey's Executor v. United States*, circumscribed the president's power to remove members of independent regulatory commissions. For a discussion of this era, see Leuchtenberg, The Supreme Court Reborn, *supra* note 20.

within the administration over how to deal with "the nine old men." It ended early in 1937, following the landslide election of 1936, when Roosevelt unveiled his infamous Court-packing scheme—his plan to pack the Court with six new members. The reaction in the country was immediate. Not even the overwhelmingly Democratic Congress—nearly four to one in the House—would go along with the scheme. Nevertheless, the Court got the message. There followed the famous "switch in time that saved nine" and the Court began rewriting the Constitution—again, without benefit of constitutional amendment.

It did so in two main steps. In 1937 the Court eviscerated the doctrine of enumerated powers. Then in 1938 it bifurcated the Bill of Rights and invented a bifurcated theory of judicial review. For the purpose of these hearings, it is one half of the 1937 step that is most important, the rewriting of the General Welfare Clause; but the rest merits a brief discussion as well, to give a more complete picture of this constitutional revolution.

In 1936, in *United States v. Butler*,[23] the Court had found the Agricultural Adjustment Act[24] unconstitutional. But in the course of doing so it opined on the great debate between Madison and Hamilton over the meaning of the so-called General Welfare Clause, coming down on Hamilton's side—yet only in dicta and hence not as law. A year later, however, following the Court-packing threat, the Court elevated that dicta as it upheld the Social Security Act[25] in *Helvering v. Davis*.[26] The words were ringing: "Congress may spend money in aid of the 'general welfare,'"[27] said the 1937 Court. Moreover, "the concept of the general welfare [is not] static. Needs that were narrow or parochial a century ago may be interwoven in our day with the well-being of the nation."[28] Thus were the floodgates opened. The modern welfare state was unleashed.

But if Congress could now engage in unbounded redistribution, so too could it regulate at will following the Court's decision that same year in *NLRB v. Jones & Laughlin Steel Corp.*[29] The issue there was the scope of Congress's power to regulate interstate commerce, a power Congress had been granted to address the impediments to interstate commerce that had arisen under the Articles of Confederation as states were imposing tariffs and other measures to protect local merchants and manufacturers from out-of-state competition. Thus, the power was meant mainly to enable Congress to ensure the free flow of goods and services among the states—to make that commerce "regular," as against state and other efforts to impede it.[30] It was not a power to regulate anything

[23] 262 U.S. 1, 65-66 (1936).
[24] 7 U.S.C.A. 601 (1933).
[25] 49 Stat. 620 (1935).
[26] 301 U.S. 619, 640 (1937).
[27] Id.
[28] Id. at 641.
[29] 301 U.S. 619 (1937); see also Wickard v. Filburn, 317 U.S. 111 (1942).
[30] See Randy E. Barnett, The Original Meaning of the Commerce Clause, 68 U. Chi. L. Rev. 101 (2000); Brief of *Amicus Curiae* Cato Institute, Jones v. United *States*, 529 U.S. 848 (2000) (visited Oct. 21, 2005) www.cato.org/pubs/legalbriefs/jvsusa.pdf.; Cf., Richard A. Epstein, The Proper Scope of the Commerce Power, 73 Va. L. Rev. 1387 (1987).

for any reason. Yet that, in effect, is what it became as the 1937 *Jones & Laughlin* Court held that Congress had the power to regulate anything that "affected" interstate commerce, which is virtually everything.

The doctrine of enumerated powers now effectively eviscerated—the floodgates open for the modern redistributive and regulatory state to pour through—only the Bill of Rights stood athwart that unbounded power. So in 1938, in famous footnote 4 of *United States v. Carolene Products*,[31] the Court addressed that impediment to Leviathan by distinguishing "fundamental" and "nonfundamental" rights, in effect, and inventing a bifurcated theory of judicial review to complement that distinction. If a law implicated "fundamental" rights like speech or voting, the Court would apply "strict scrutiny" and would doubtless find it unconstitutional. By contrast, if a law implicated "nonfundamental" rights like property, contract, or the rights we exercise in ordinary commercial relations, the Court would uphold the law as long as there was some "rational basis" for it.[32] That judicial deference to the political branches regarding economic rights, coupled with strict scrutiny for political rights, amounted to the democratization and to the politicization of the Constitution, to opening the door to political control of economic affairs, public and private alike, beyond anything the Framers could have imagined.[33]

The rest is history, as we say, with redistributive and regulatory schemes, federal, state, and local, pouring forth. Others on this panel can testify as to the numbers that illustrate that explosion in government programs. My concern, rather, is to outline how it happened that under a Constitution meant to limit government we got a government of effectively unlimited power.

Toward that end, and beyond the history of the matter, let me add that most of the spending that is the focus of these hearings has arisen under the so-called General Welfare Clause, which the Court has also referred to as the Spending Clause. In truth, however, there are no such clauses in the Constitution,[34] which is why I have invoked the term "so-called." A careful reading of the first of Congress's 18 enumerated powers, which is the nominal source of those so-called clauses, coupled with reflection on the structure of the document, will reveal merely a power to tax at the head of Article I, section 8, much as the second of Congress's enumerated powers is the power to borrow. If Congress exercises either or both of those powers—or its Article IV power to "dispose" of public lands, for that matter—and it wants then to appropriate and spend the proceeds on any of the ends that are authorized to it, it must do so under the Necessary and Proper Clause. For taxing, borrowing, disposing, appropriating, and spending are distinct powers. The first three are expressly authorized to Congress. Appropriating and spending, by contrast, are necessary and proper *means* toward executing the powers authorized to the government—means provided for under the Necessary and Proper

[31] 304 U.S. 104 (1938). For a devastating critique of the politics behind the *Carolene Products* case, see Geoffrey P. Miller, The True Story of *Carolene Products*, 1987 Sup. Ct. Rev. 397.
[32] I have discussed that methodology in Roger Pilon, Foreword: Substance and Method at the Court, 2002-2003 Cato Sup. Ct. Rev. vii. (2003).
[33] See Bernard H. Siegan, Economic Liberties and the Constitution (1980).
[34] See Gary Lawson, Making a Federal Case Out of It: *Sabri v. United States* and the Constitution of Leviathan. 2003-2004 Cato Sup. Ct. Rev. 119 (2004).

Clause. As such, they are not *independent* but only *instrumental* powers, exercised in service of ends *that in turn limit their use to those ends*. Put simply, Congress cannot appropriate and spend for any end it wishes, but only for those ends it is authorized to pursue—and they are, as Madison said, "few and defined."

We come, then, to the nub of the matter. Search the Constitution as you will, you will find no authority for Congress to appropriate and spend federal funds on education, agriculture, disaster relief, retirement programs, housing, health care, day care, the arts, public broadcasting—the list is endless. That is what I meant at the outset when I said that most of what the federal government is doing today is unconstitutional because done without constitutional authority. Reducing that point to its essence, the Constitution says, in effect, that everything that is not authorized—to the government, by the people, through the Constitution—is forbidden. Progressives turned that on its head: Everything that is not forbidden is authorized.

But don't take my word for it. Take the word of those who engineered the constitutional revolution. Here is President Roosevelt, writing to the chairman of the House Ways and Means Committee in 1935: "I hope your committee will not permit doubts as to constitutionality, however reasonable, to block the suggested legislation."[35] And here is Rexford Tugwell, one of the principal architects of the New Deal, reflecting on his handiwork some thirty years later: "To the extent that these new social virtues [i.e., New Deal policies] developed, they were tortured interpretations of a document [i.e., the Constitution] intended to prevent them."[36] They knew exactly what they were doing—turning the Constitution on its head. That is the legacy we live with today.

**Implications of the Constitutional Revolution**

That legacy has many implications. Let me distinguish five. First, and perhaps most important, is the loss of legitimacy—moral, political, and legal. Today, we tend to think mainly of political legitimacy, failing to see how the several grounds of legitimacy go together. We imagine that the people, by their periodic votes, tell the government what they want; and to the extent that it responds to that expression of political will, consistent with certain state immunities and individual rights that might check it, the government and its actions are legitimate. Whatever moral legitimacy flows from that view is a function of the moral right of self-government, but that right is largely open-ended regarding the arrangements it might produce. It could produce limited government. But it

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[35] Letter from Franklin D. Roosevelt to Rep. Samuel B. Hill (July 6, 1935), in 4 *The Public Papers and Addresses of Franklin D. Roosevelt* 91-92 (Samuel I. Rosenman ed., 1938).

[36] Rexford G. Tugwell, A Center Report: Rewriting the Constitution, Center Magazine, March 1968, at 20. This is a fairly clear admission that the New Deal was skating not simply on thin ice but on no ice at all. For comments from the other side, see, e.g., Gary Lawson, The Rise and Rise of the Administrative State, 107 Harv. L. Rev. 1231 (1994): "The post-New Deal administrative state is unconstitutional, and its validation by the legal system amounts to nothing less than a bloodless constitutional revolution;" Richard A. Epstein, Commerce Clause, *supra* note 30, at 1388: "I think that the expansive construction of the [commerce] clause accepted by the New Deal Supreme Court is wrong, and clearly so."

could as easily produce unlimited government.[37] And without a keen sense of the role and place of moral legitimacy, we are indifferent as to which it is.

That view characterizes legitimacy in a parliamentary system, more or less; it is not how legitimacy operates in our constitutional republic. Rather, as shown by the Declaration of Independence, the main principles of which shaped the Constitution, we find our roots in Lockean state-of-nature theory and its underlying theory of natural rights.[38] Legitimacy is first defined by the moral order, by the rights and obligations we have with respect to each other. Only then do we turn to political and legal legitimacy, through the social contract—the Constitution—that facilitates and reflects it. As outlined earlier, the federal government gets its powers by delegation from the people through ratification—reflecting mainly the (natural) powers the people have to give it—not through subsequent elections, which are designed primarily to fill elective offices. To be sure, many of the powers thus delegated leave room for discretion by those elected. That is why elections matter: different candidates may have different views on the exercise of that discretion—the discretion to declare war, to take a clear example. But through elections the people can no more give government a power it does not have than they can take from individuals a right they do have. In a constitutional republic like ours, it is the Constitution that sets the powers, not the people through periodic elections.

But when powers or rights are expanded or contracted not through ratification but through elections and the subsequent actions of elected officials, and the courts fail to check that, the Constitution is undermined and the powers thus created are illegitimate. That happened when the New Deal Court bowed to the political pressure brought on by Roosevelt's Court-packing threat. And that paved the way for powers that have never been *constitutionally* authorized by the people—for illegitimate powers, that is—and for the accompanying loss of rights.

Some would argue that we could correct that problem of illegitimacy simply by putting our present arrangements to a vote through the supermajoritarian amendment and ratification procedures provided for in Article V. Were that vote successful, that would indeed produce political and legal legitimacy. But because the Constitution as it stands

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[37] That was pretty much the view of Justice Holmes in his famous dissent in *Lochner v. New York*, 198, U.S. 45 (1905). Declaring that the case was "decided upon an economic theory which a large part of the country does not entertain," and adding that his "agreement or disagreement [with the theory] has nothing to do with the right of a majority to embody their opinions in the law," Holmes proceeded to read out of the Constitution all economic substance: "a constitution is not intended to embody a particular economic theory, whether of paternalism and the organic relation of the citizen to the state or of laissez faire." Id. at 75. But we find a similar view in many modern conservatives as well. Thus, Robert H. Bork speaks of the "two opposing principles" of what he calls the "Madisonian dilemma." Our first principle, Bork says, "is self-government, which means that in wide areas of life majorities are entitled to rule, if they wish, simply because they are majorities. The second is that there are nonetheless some things majorities must not do to minorities, some areas of life in which the individual must be free of majority rule." Robert H. Bork, The Tempting of America 139 (1990). That gets Madison exactly backward. Madison's vision was that in *wide* areas of life individuals are entitled to be free simply because they are born free. Nonetheless, in *some* areas majorities are entitled to rule because we have authorized them to rule, giving them powers "few and defined."

[38] John Locke, The Second Treatise of Government, in Two Treatises of Government (1960) (1690).

today reflects fairly closely, in my judgment, the moral order that can be justified—in other words, the Framers and those who subsequently amended the document got it right, for the most part—I would object to amending the Constitution simply to lend political and legal legitimacy to the modern welfare state. Better, I believe, to be able to point not simply to that state's moral illegitimacy but to its political and legal illegitimacy as well.

The second untoward implication of our departure from the Constitution is the chaos that follows for law more generally.[39] The judicial methodology the Constitution contemplates for most constitutional questions is really quite simple. Assuming a court has jurisdiction in a case challenging a given federal statute, the first question is whether Congress had authority to enact the statute. If not, that ends the matter. If yes, the next question is whether and how the act may implicate rights, enumerated or unenumerated.

Those questions are not always easy to answer and often involve close calls. But the difficulties are multiplied exponentially when the floodgates are opened and federal, state, and local legislation pours through, producing often inconsistent and incoherent "law" from every direction. Add to that, as noted above, the tendentious and politicized judicial methodology that flowed from *Carolene Products*—today we have three and sometimes four "levels" of judicial review,[40] each with its own standards, and multi-factored "balancing" tests—and it soon becomes clear that we are far removed from a Constitution that was written to be understood at least by the educated layman. Life is complicated enough on its own terms. When government intrudes in virtually every corner of life, the complications can easily become overwhelming and unbearable. The Constitution was meant to bring order. If under it "anything goes," order goes too, and chaos follows.

Closely related to those two implications is a third: disrespect for the Constitution entails disrespect for the rule of law itself. If Congress can redistribute and regulate virtually at will, unrestrained by the limits the Constitution imposes, the rule of law is at risk. By definition, unauthorized powers intrude on rights retained by the people; but a cavalier attitude toward powers can lead more directly to the same attitude toward rights: if powers can be expanded with impunity, so too can rights be contracted.[41] In fact, a "living constitution," interpreted to maximize political discretion, can be worse than no constitution at all, because it preserves the patina of constitutional legitimacy while unleashing the political forces that a constitution is meant to restrain. And how long can "anything goes" for officials go unnoticed by the citizenry? A general decline in respect for law must follow.

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[39] I have discussed this issue more fully in Roger Pilon, Foreword: Can Law this Uncertain Be Called Law? 2003-2004 Cato Sup. Ct. Rev. vii (2004).

[40] For my critique of an opinion by Justice Anthony Kennedy distinguishing four "levels" of review, *Turner Broadcasting System v. FCC*, 512 U.S. 622 (1994), see Roger Pilon, A Modest Proposal on "Must-Carry," the 1992 Cable Act, and Regulation Generally: Go Back to Basics, 17 Hastings Comm/Ent. L.J. 41 (1994).

[41] That is arguably what happened in *McConnell v. FEC*, 124 S. Ct. 619 (2003), upholding the McCain-Feingold Campaign Finance Act, 116 Stat. 81 (2002), which President George W. Bush signed while saying it was unconstitutional. See Eric S. Jaffee, *McConnell v. FEC*: Rationing Speech to Prevent "Undue Influence," 2003-2004 Cato Sup. Ct. Rev. 245 (2004).

Fourth, when constitutional integrity declines we lose the discipline a constitution is designed to impose on government. A constitution makes it harder for government to act, which is one of the main reasons for having one. This implication speaks to one of the basic functions of a constitution, which is not only to empower but to *limit* the government that is created through it. In the original position, when we created and ratified the Constitution, we agreed to limit the government's power as an act of self-discipline. We could have set no limits on the government's power, of course; but that would have left us to a future determined by the political winds, and experience had taught us the perils of that course. Thus, we struck what we thought was a careful balance, giving the government enough power to do what we thought it should do, but reserving to ourselves the liberty appropriate to a free people. With that balance struck, the Constitution would serve to discipline us and future generations who might be tempted, given the circumstances, to grant the government more power than, in our considered judgment, we thought prudent.

Future generations could adjust that balance, of course, by amending the Constitution, provided sufficient numbers among them wanted to do so. In fact, that is just what happened following the Civil War. Troubled as the Framers were about the institution of slavery, which they recognized only obliquely in the Constitution to ensure union, they left its regulation to the states. After the Civil War, however, a new generation not only abolished slavery but, through the Fourteenth Amendment, fundamentally changed the balance between the federal government and the states. With the ratification of that amendment we finally had federal remedies against state violations of our rights.[42] Thus, although the amendment is properly read as having expanded *federal* power, it was done to discipline *state* power. A new balance was struck, to be sure, but because it was done through the constitutional process it did not amount to abandoning the discipline a constitution imposes, which is what happens when we stray from the document's principles. In fact, the contrast between the different ways in which the Civil War and the New Deal generations changed the rules is stark and instructive. The Civil War generation did it the right way—through the ratification process. The New Deal generation, faced with a choice between amending the Constitution and changing it by judicial legerdemain, chose the latter.

But the larger picture regarding discipline should not be lost. For just as the Constitution disciplines the government, so too it disciplines the people in their daily lives. Professor Warren captures that point nicely with a quote from South Carolina's Warren R. Davis, speaking in the House on April 4, 1832:

> This system of transferring property by legislation—of giving pensions and gratuities to individuals, companies, corporations, and the States— ... will degrade the States by inducing them to look for bounties, to the Federal Government; will degrade and demoralize the people, by making them dependent

[42] See Robert J. Reinstein, Completing the Constitution: The Declaration of Independence, Bill of Rights, and Fourteenth Amendment, 47 Temp. L. Rev. 361 (1993). In 1833 the Court had ruled that the Bill of Rights applied only against the government created by the document (the U.S. Constitution) to which it was appended. Barron v. Mayor and City Council of Baltimore, 32 U.S. 243 (1833).

> on the Government; will emasculate the free spirit of the country .... As soon as the people of ancient Rome were taught to look to the public granaries for support, the decay of public virtue was instantaneous.[43]

Vast numbers of Americans today look to Washington for a rich array of "entitlements" that speak of nothing so much as the illusion of something for nothing. And politicians nurture that illusion, propelling us all in the downward spiral that Thomas Hobbes aptly called a war of all against all. Stated otherwise, as contributors to public largesse become fewer and recipients more numerous, the downward spiral becomes a death spiral. And we are headed in that direction as discipline continues to erode.

Finally, and closely related, let me little more than mention the economic implications of effectively unlimited government as I expect that others on the panel will address those more fully. By this point in human history, and especially after the collapse of the socialist experiments of the 20th century, we have a fairly clear understanding of the connection between liberty and prosperity—a connection that Adam Smith articulated so well in 1776,[44] and economists like Mises, Hayek, and Friedman, among many others, have refined and extended in our own time. What that understanding points to, once again, is the prescience of the Framers in drafting a constitution dedicated to securing our liberty and hence our extraordinary prosperity. But neither liberty nor prosperity is guaranteed by a mere parchment, especially by one that is ignored. The American economy has proven resilient enough to withstand the blows imposed by the galloping government of the 20th century—although we will never know how much more prosperous we might have been had that government been better reined. In future, however, to the extent we ignore the lessons of economics we invite the consequences that have befallen so many other nations that have chosen economic planning over economic liberty. And the basic lesson of economics is that liberty, property, and contract are the fundamental preconditions of prosperity.

**What Is to Be Done?**

We did not create our overextended, unconstitutional government overnight. We cannot restore constitutional government overnight—too many people have come to rely on the irresponsible promises that have been made. But we can begin the process of restoration. For that, the most important thing to do now is to start restoring a constitutional ethos in the nation. And that should be the business of all branches, not simply the Court, which can hardly do the job by itself, even if it were the right body to do so. What we have here, in short, is not simply or even mainly a legal problem. Rather, it is a political and, more deeply still, a moral problem.

Because I have discussed what needs to be done in some detail in chapter 3 of the *Cato Handbook on Policy*,[45] copies of which are available in every congressional office, I will simply outline those proposals here.

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[43] Warren, Santa Claus, *supra* note 13, front page, citing only to 22d Cong., 1st Sess.
[44] Adam Smith, An Inquiry Into the Nature and Causes of the Wealth of Nations (1776).
[45] Roger Pilon, Congress, the Courts, and the Constitution, ch. 3, in Cato Handbook on Policy (2005).

Limits on government today, when we've had them, have come largely from political and budgetary rather than from constitutional considerations. It has not been because of any perceived lack of constitutional authority that government in recent years has failed to undertake a program but because of practical limits on the power of government to tax and borrow—and even those limits have failed in times of economic prosperity. To restore truly limited government, therefore, we have to do more than define the issues as political or budgetary. We have to go to the heart of the matter and raise the underlying constitutional questions. In a word, we have to ask the most fundamental question of all: Does the government have the authority, the constitutional authority, to do what it is doing?

That means, of course, that we are going to have to come to grips with the present state of public debate on the subject. It surely counts for something that a substantial number of Americans—to say nothing of the organs of public opinion—have little apprehension of or appreciation for the Constitution's limits on activist government. Thus, when thinking about how and how fast to reduce government, we have to recognize that the Court, after nearly 70 years of arguing otherwise, is hardly in a position, by itself, to relimit government in the far-reaching way a properly applied Constitution requires. But neither does Congress at this point have sufficient moral authority, even if it wanted to, to end tomorrow the vast array of programs it has enacted over the years with insufficient constitutional authority.

For either Congress or the Court to be able to do fully what should be done, therefore, a proper foundation must first be laid. In essence, the climate of opinion must be such that a sufficiently large portion of the American public stands behind the changes that are undertaken. When enough people come forward to ask—indeed, to demand—that government limit itself to the powers it is given in the Constitution, thereby freeing individuals, families, and communities to solve their own problems, we will know we are on the right track.

Fortunately, a change in the climate of opinion on such basic questions has been under way for some time now. The debate today is very different than it was in the 1960s and 1970s. But there is a good deal more to be done before Congress and the courts are able to move in the right direction in any far-reaching way.

To continue the process, Congress should take the lead by engaging in constitutional debate in Congress, much as happened in the 19th century, thereby encouraging constitutional debate in the nation. That was urged by the House Constitutional Caucus during the 104th Congress. Under the leadership of House freshmen like J. D. Hayworth and John Shadegg of Arizona, Sam Brownback of Kansas, and Bob Barr of Georgia, together with a few more senior congressmen like Richard Pombo of California, an informal Constitutional Caucus was established in the "radical" 104th Congress. Unfortunately, the caucus has been moribund since then. It needs to be revived—along with the spirit of the 104th Congress—and its work needs to be expanded.

By itself, of course, neither the caucus nor the entire Congress can solve the problem before us. To be sure, in a reversal of all human experience, Congress in a day could agree to limit itself to its enumerated powers and then roll back the countless programs it has enacted by exceeding that authority. But it would take authoritative opinions from the Supreme Court, reversing a substantial body of largely post-New Deal decisions, to embed those restraints in "constitutional law"—even if they have been embedded in the Constitution from the outset, the Court's modern readings of the document notwithstanding.

The ultimate goal of the caucus and Congress, then, should be to encourage the Court to reach such decisions. But history teaches, as noted above, that the Court does not operate entirely in a vacuum—that to some degree public opinion is the precursor and seedbed of its decisions. Thus, the more immediate goal of the caucus should be to influence the debate in the nation by influencing the debate in Congress. To do that, it is not necessary or even desirable, in the present climate, that every member of Congress be a member of the caucus—however worthy that end might ultimately be—but it is necessary that those who join the caucus be committed to its basic ends. And it is necessary that members establish a clear agenda for reaching those ends.

To reduce the problem to its essence, every day members of Congress are besieged by requests to enact countless measures to solve endless problems. Indeed, one imagines that no problem is too personal or too trivial not to warrant *federal* attention, no less. Yet most of the "problems" Congress spends most of its time addressing—from health care to day care to retirement security to economic competition—are simply the personal and economic problems of life that individuals, families, and firms, not governments, should be addressing—quite apart from the absence of constitutional authority to address them.

Properly understood and used, then, the Constitution can be a valuable ally in the efforts of the caucus and Congress to reduce the size and scope of government. For in the minds and hearts of most Americans, it remains a revered document, however little it may be understood by a substantial number of them.

If the Constitution is to be thus used, however, the principal misunderstanding that surrounds it must be recognized and addressed. In particular, the modern idea that the Constitution, without further amendment, is an infinitely elastic document that allows government to grow to meet public demands of whatever kind must be challenged. More Americans than presently do must come to appreciate that the Framers, who were keenly aware of the expansive tendencies of government, wrote the Constitution precisely to check that kind of thinking and that possibility. To be sure, they meant for government to be our servant, not our master, but they meant it to serve us in a very limited way—by securing our rights, as the Declaration of Independence says, and by doing those few other things that government does best, as spelled out in the Constitution.

In all else, as discussed above, we were meant to be free—to plan and live our own lives, to solve our own problems, which is what freedom is all about. Some may characterize that vision as tantamount to saying, "You're on your own," but that kind of response simply misses the point. In America individuals, families, and organizations have never been "on their own" in the most important sense. They have always been members of communities, of civil society, where they could live their lives and solve their problems by following a few simple rules about individual initiative and responsibility, respect for property and promise, and charity toward the few who need help from others. Massive government planning and programs have upset that natural order of things—less so in America than elsewhere, but very deeply all the same.

Those are the issues that need to be discussed, both in human and in constitutional terms. We need, as a people, to rethink our relationship to government. We need to ask not what government can do for us but what we can do for ourselves and, where necessary, for others—not through government but apart from government, as private citizens and organizations. That is what the Constitution was written to enable. It empowers government in a very limited way. It empowers people—by leaving them free—in every other way.

To proclaim and eventually secure that vision of a free people, the Constitutional Caucus should reconstitute itself and rededicate itself to that end in the 109th Congress and at the beginning of every Congress hereafter. Standing apart from Congress, the caucus should nonetheless be both of and above Congress—as the constitutional conscience of Congress. Every member of Congress, before taking office, swears to support the Constitution—hardly a constraining oath, given the modern Court's open-ended reading of the document. Members of the caucus should dedicate themselves to the deeper meaning of that oath. They should support the Constitution the Framers gave us, as amended by subsequent generations, not as "amended" by the Court's expansive interpretations.

Acting together, the members of the caucus could have a major impact on the course of public debate in this nation—not least, by virtue of their numbers. What is more, there is political safety in those numbers. As Benjamin Franklin might have said, no single member of Congress is likely to be able to undertake the task of restoring constitutional government on his own, for in the present climate he would surely be hanged, politically, for doing so. But if the caucus hangs together, the task will be made more bearable and enjoyable—and a propitious outcome made more likely.

On the agenda of the caucus, then, should be those specific undertakings that will best stir debate and thereby move the climate of opinion. Drawn together by shared understandings, and unrestrained by the need for serious compromise, the members of the caucus are free to chart a principled course and employ principled means, which they should do.

They might begin, for example, by surveying opportunities for constitutional debate in Congress, then making plans to seize those opportunities. Clearly, when new bills are introduced, or old ones are up for reauthorization, an opportunity is presented to debate constitutional questions. But even before that, when plans are discussed in party sessions, members should raise constitutional issues. Again, the caucus might study the costs and benefits of eliminating clearly unconstitutional programs, the better to determine which can be eliminated most easily and quickly.

Above all, the caucus should look for strategic opportunities to employ constitutional arguments. Too often, members of Congress fail to appreciate that if they take a principled stand against a seemingly popular program—and state their case well—they can seize the moral high ground and prevail ultimately over those who are seen in the end to be more politically craven.

All of that will stir constitutional debate—which is just the point. For too long in Congress that debate has been dead, replaced by the often dreary budget debate. This nation was not established by men with green eyeshades. It was established by men who understood the basic character of government and the basic right to be free. That debate needs to be revived. It needs to be heard not simply in the courts—where it is twisted through modern ''constitutional law''—but in Congress as well.

Before concluding, Mr. Chairman, let me leave the subcommittee with three basic recommendations, which I have discussed more fully in the *Cato Handbook* I referenced above:

- Enact nothing without first consulting the Constitution for proper authority and then debating that question on the floors of the House and the Senate.
- Move toward restoring constitutional government by carefully returning power wrongly taken over the years from the states and the people.
- Reject the nomination of judicial candidates who do not appreciate that the Constitution is a document of delegated, enumerated, and thus limited powers.

**Conclusion**

America is a democracy in the most fundamental sense of that idea: authority, or legitimate power, rests ultimately with the people. But the people have no more right to tyrannize each other through democratic government than government itself has to tyrannize the people. When they constituted us as a nation by ratifying the Constitution and the amendments that have followed, our forefathers gave up only certain of their powers, enumerating them in a written constitution. We have allowed those powers to expand beyond all moral and legal bounds—at the price of our liberty and our well-being. The time has come to return those powers to their proper bounds, to reclaim our liberty, and to enjoy the fruits that follow.

COMMITTEE HEARING

Guns & Butter: Setting Priorities in Federal Spending in the Context of Natural Disaster, Deficits and War:
October 25, 2005

# The Economic Consequences of Government Spending

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Economic theory does not necessarily tell us the proper size of government. Instead, economic theory tells us to examine costs and benefits in order to determine whether resources are allocated in a manner that increases or decreases economic growth.

Economists are fond of stating that there is no such thing as a free lunch. For purposes of fiscal policy, this means that a dollar that is spent by the government is a dollar that no longer is available to the private sector of the economy. This is an unavoidable cost. The key question is whether there are offsetting benefits.

Not all government spending is created equal. Some forms of spending on "public goods" facilitate the operation of a market economy. A well-functioning legal system, for instance, is necessary to facilitate private contracts. There will be an economic cost when resources are taken from the private sector to finance outlays for a court system, but the benefits presumably will exceed those costs – meaning that the net effect on economic performance is positive.

Other forms of government spending have a less desirable impact on economic activity. If a program does not facilitate or encourage economic activity, or has only a small positive effect, then the aggregate impact on the economy will be negative because there are limited benefits – if any – to outweigh the costs. And if the program actually undermines work, saving, and investment or encourages misallocation of resources, then the overall adverse impact on economic growth will be particularly pronounced. A good example from recent events is federal flood insurance. Not only does the program require resources to be taxed or borrowed from the productive sector of the economy – with all the associated economic costs, but it also encourages over-building in flood zones, which leads to the destruction of wealth during natural disasters.

There are two macroeconomic reasons why government spending can undermine economic performance. The first reason, mentioned above, is "resource displacement." Every time government spends money, it is using labor and/or capital and those resources no longer are available for private sector uses.

The second macroeconomic issue associated with government spending is the "financing cost." When government taxes, it not only takes money from the productive sector, but it also raises revenue by means of a tax system that generally reduces incentives to work, save, and invest. And if it finances spending with debt, it siphons money out of private credit markets.

The microeconomic costs of government spending involve the impact of various forms of budget outlays. The two most important of these effects are the "subsidy for sub-optimal behavior" and the "penalty for pro-growth behavior." In the first instance, some government programs are directly linked to choices that reduce economic performance. Prior to welfare reform, for instance, income transfer programs frequently rewarded people for choosing not to work or for having children out of wedlock.

In the second instance, specific government programs discourage behaviors that are good for the economy. A large number of government programs, for example, reduce incentives to save by subsidizing health care, retirement, education, and housing. Other programs reduce incentives to work.

Other forms of microeconomic damage are associated with outlays – such as budgets for regulatory agencies – that result in the imposition of costs on private sector activity. A recent example is the Sarbanes-Oxley legislation. The actual budget costs for the Securities and Exchange Commission is only a fraction of the economic costs associated with the regulatory burden generated by that single piece of legislation.

Another form of microeconomic damage involves the misallocation of resources. Education is widely considered a public good, yet there is considerable evidence that the means of delivering that public good is very inefficient because government school monopolies provide a very low amount of educational achievement per dollar spent.

The economic impact of government spending can be presented in graphical form. The so-called Rahn Curve in Figure 1 (attached) shows that economic output or growth is very low when government is non-existent. In this anarchical world, workers, savers, investors, and entrepreneurs do not have an environment conducive to productive behavior.

As certain public goods are provided, however, economic growth and/or output rises. There is a growth-maximizing level of government spending. But once outlays exceed that point, economic performance begins to slip. And as government becomes bigger and bigger, the economy suffers larger losses of output and/or growth.

This theoretical construct is the spending equivalent of the Laffer Curve. In both cases, the extreme points on the curve show adverse consequences. The more challenging question, of course, is figuring out whether government is too big or too small. In other words, where is America on the Rahn Curve?

This is a difficult question, but empirical data and academic research indicate that excessive government has a negative impact on economic performance. A comparison of US and European fiscal and economic outcomes can be very instructive. As seen in Figure 2 (attached), the average burden of government in the European Union is much larger than it is in the United States. What has this meant for economic performance?

- Per capita economic output in the U.S. is more than 40 percent higher than the average for EU–15 nations.
- Real economic growth in the U.S. has been more than 50 percent faster than EU–15 growth during the past 10 years.
- The U.S. unemployment rate is significantly lower than the EU–15 unemployment rate, and there is a stunning gap in figures for long-term unemployment.

These cross-country comparisons are instructive, but the academic research is even more conclusive. In the past 20 years, a wealth of scholarly research has found a negative link between government spending and economic output. To cite just a few examples:

- A *Public Choice* study reported: "[A]n increase in GTOT [total government spending] by 10 percentage points would decrease the growth rate of TFP [total factor productivity] by 0.92 percent [per annum]. A commensurate increase of GC [government consumption spending] would lower the TFP growth rate by 1.4 percent [per annum]."
- A National Bureau of Economic Research paper stated: "A reduction by one percentage point in the ratio of primary spending over GDP leads to an increase in investment by 0.16 percentage points of GDP on impact, and a cumulative increase by 0.50 after two years and 0.80 percentage points of GDP after five years. The effect is particularly strong when the spending cut falls on government wages: in response to a cut in the public wage bill by 1 percent of GDP, the figures above become 0.51, 1.83 and 2.77 per cent respectively."
- A study from the *Journal of Monetary Economics* stated: "We also find a strong negative effect of the growth of government consumption as a fraction of GDP. The coefficient of –0.32 is highly significant and, taken literally, it implies that a one standard deviation increase in government growth reduces average GDP growth by 0.39 percentage points."
- A National Bureau of Economic Research paper stated: "[A] 10 percent balanced budget increase in government spending and taxation is predicted to reduce output growth by 1.4 percentage points per annum, a number

comparable in magnitude to results from the one-sector theoretical models in King and Robello."

- A *Journal of Macroeconomics* study discovered: "[T]he coefficient of the additive terms of the government-size variable indicates that a 1% increase in government size decreases the rate of economic growth by 0.143%."

- A study in *Public Choice* reported: "[A] one per-cent increase in government spending as a per-cent of GDP (from, say, 30 to 31%) would raise the unemployment rate by approximately .36 of one percent (from, say, 8 to 8.36 percent)."

- A study in the *European Economic Review* reported: "The estimated effects of GEXP [government expenditure variable] are also some-what larger, implying that an increase in the expenditure ratio by 10 percent of GDP is associated with an annual growth rate that is 0.7–0.8 percentage points lower."

Finally, it is worth commenting on specific examples of nations that have prospered by reducing the burden of government. Ireland is best know for sweeping tax rate reductions, but government spending also was reduced from more than 50 percent of GDP to about 35 percent of GDP. The former "sick man of Europe" is now known as the Celtic Tiger. Unemployment has dropped from 17 percent to 5 percent, and Ireland is now the second-richest nation in the European Union.

New Zealand enjoyed similar success, reducing burden of government by an equally dramatic amount. The economy has turned around and is now rated as one of the most competitive in the world. Slovakia is an example from the former Soviet Bloc. In a remarkably short period of time, government spending has been reduced by about 20 percentage points of GDP according to OECD data. Combined with other economic reforms, Slovakia now leads the world in foreign direct investment per capita.

This testimony provides just a brief glance at some of the theoretical, empirical, and academic evidence that excessive government hinders economic performance. This is a critically important issue for the future of American competitiveness. In recent years, policy makers have allowed a record increase in government spending. In all likelihood, this spending is causing the economy to grow slower than would otherwise be the case.

But this short-term spending increase is a drop in the bucket compared to long-terms threats. Demographic changes – combined with misguided decisions such as the creation of a new entitlement for prescription drugs – mean that government will consume a growing share of America's economic output.

If government is allowed to expand to levels found in Europe's welfare states, it is unavoidable that America will suffer the economic weakness now plaguing nations such as France and Germany.

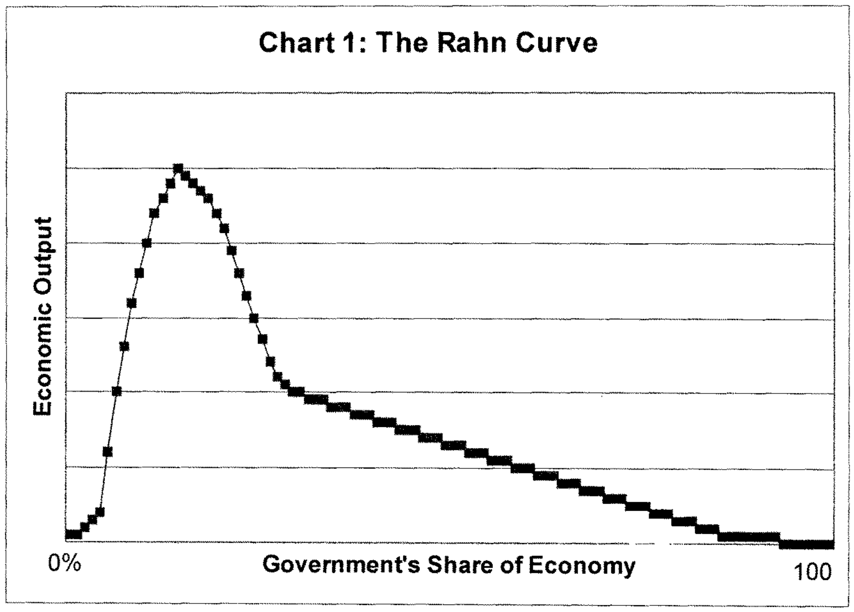
Chart 1: The Rahn Curve
Economic Output
0%
Government's Share of Economy
100

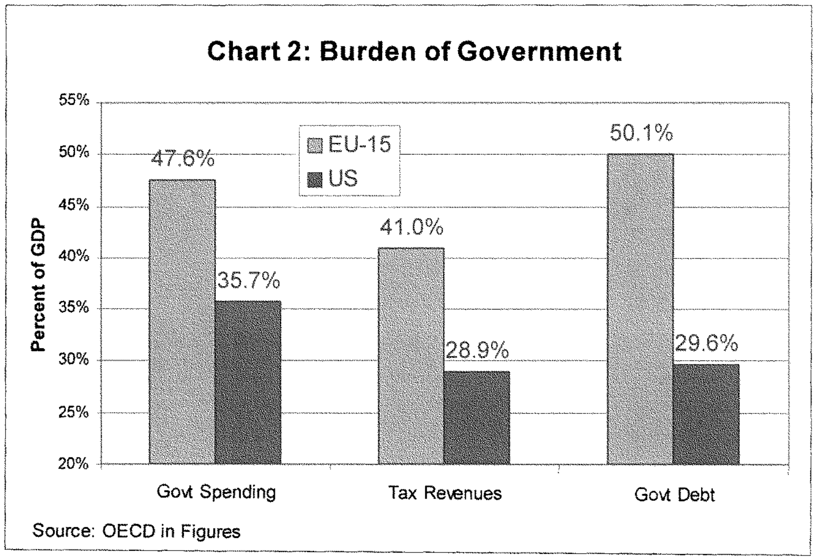
Chart 2: Burden of Government
55%
50%
45%
40%
35%
30%
25%
20%
Percent of GDP
EU-15
US
47.6%
35.7%
41.0%
28.9%
50.1%
29.6%
Govt Spending
Tax Revenues
Govt Debt
Source: OECD in Figures